

Tutorial Letter 201/1/2018

The Internal Audit Process: Planning the engagement

AUI3701

Semester 1

Department of Auditing

This tutorial letter contains important information about your module.

Bar code

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1 BRIEFING

This assignment consisted of 20 multiple-choice questions which you had to answer on a mark-reading sheet. The assignment was marked electronically and you should have received a report on the mark you obtained for the assignment. At this stage we would like to provide the correct answers to the various questions.

The mark you received for this assignment will contribute towards your year mark, and your year mark will contribute 10% towards your final mark for this module.

We trust that you found this assignment interesting and challenging. We hope you are looking forward to learning more about the practice of internal auditing in this module.

Lecturer: AUI3701

2 KEY TO ASSIGNMENT 01/2018 (FIRST SEMESTER)

Note the following in the comments below:

The **Standards** refers to the International Standards for the Professional Practice of Internal Auditing

CAE stands for the chief audit executive

IAA stands for the internal audit activity

Question	Correct answer	Study guide reference
1.1	3	Learning unit 5.3.3
<p>Option 3 is correct.</p> <p>Option 1, 3 and 4 is incorrect. Transactions for specific cardholders, high-monetary value transactions and the suppliers used by each cardholder will be identified using generalised audit software.</p>		
Question	Correct answer	Study guide reference
1.2	2	Learning unit 7.2
<p>Option 2 is correct. An engagement objective is a broad statement developed by internal auditors to define intended engagement accomplishments. Determining whether inventory stocks are sufficient to meet projected sales is an engagement objective because it defines an audit accomplishment, not an engagement procedure. A procedure is designed to gather information that corroborates and documents conclusions about objectives.</p>		

Option 1 is incorrect. Observation of inventory is an engagement procedure.

Option 3 is incorrect. Calculation of inventory turnover is an engagement procedure.

Option 4 is incorrect. Inclusion of stockout information is a specification for an engagement communication.

Question	Correct answer	Study guide reference
1.3	1	Learning unit 3.1.2.1

Option 1 is correct. Enterprise risk management (ERM) is a process, effected by an entity's board of directors, management, and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives. The emphasis is on the objectives of a specific entity and establishing a means for evaluating the effectiveness of ERM.

Option 2 is incorrect. ERM is concerned with selecting not the best risk response but the risk response that falls within the enterprise's risk tolerances and appetite.

Option 3 is incorrect. Risk management processes cannot guarantee achievement of objectives.

Option 4 is incorrect. Involvement of internal auditors in establishing control activities impairs their independence and objectivity.

Question	Correct answer	Study guide reference
1.4	3	Learning unit 1

Option 3 is correct. Rule of Conduct 4.3 states that the "Internal auditors shall continually improve their proficiency and the effectiveness and quality of their service." The internal auditor did not engage in continuing professional education.

Options 2, 3 and 4 are incorrect because these actions are allowable under the Code of Ethics.

Question	Correct answer	Study guide reference
1.5	1	Learning unit 2

Option 1 is correct.

Option 2 is incorrect. This is when engagement information is sufficient.

Option 3 is incorrect. This is when engagement information is reliable.

Option 4 is incorrect. A person can be objective and unbiased, but information cannot have these qualities.

Question	Correct answer	Study guide reference
1.6	4	Learning unit 7.1

Option 4 is correct. Senior management is charged with overseeing the establishment, administration, and evaluation of the processes of risk management and control. Operating manager's responsibilities include assessment of the risks and controls in their units. Internal and external auditors provide varying degrees of assurance about the state of effectiveness of the risk management and control processes of the organisation.

Option 1 is incorrect. Operating managers' responsibilities include assessment of the risk management and control.

Option 2 is incorrect. Internal auditors provide varying degrees of assurance about the state of effectiveness of the risk management and control processes of the organisation.

Option 3 is incorrect. External auditors provide varying degrees of assurance about the state of effectiveness of the risk management and control processes of the organisation.

Question	Correct answer	Study guide reference
1.7	3	Learning unit 6.2

Option 3 is correct.

Option 1 is incorrect. An audit risk is the risk that the auditor might not identify critical information during an audit.

Option 2 is incorrect. This is an example of a residual risk.

Option 4 is incorrect. Control risk is when an error may not be detected and corrected or prevented by the entity's internal control mechanism.

Question	Correct answer	Study guide reference
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1.8	1	Learning unit 6.2.2
<p>Option 1 is correct. Refer to the Study guide for a list of responsibilities of the internal auditor with relation to fraud.</p> <p>Option 2, 3 and 4 is incorrect.</p>		
Question	Correct answer	Study guide reference
1.9	1	Learning unit 1
<p>Option 1 is correct. According to the Definition of Internal Auditing, “Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.”</p> <p>Option 2 is incorrect. Performing the functions of design and implementation of risk management and control systems would impair the objectivity of the internal auditors. An internal auditor may recommend control standards and review procedures prior to their implementation.</p> <p>Option 3 is incorrect. Internal auditing is much broader than examining and evaluating an organisation’s accounting system.</p> <p>Option 4 is incorrect. Internal auditing serves the organisation, not the external auditors.</p>		
Question	Correct answer	Study guide reference
1.10	4	Learning unit 2
<p>Option 4 is correct. The charter establishes the internal auditor to contact units outside the organisation, including the nature of the CAE’s functional reporting relationship with the board; authorises access to records, personnel, and physical properties relevant to the performance of engagements; and defines the scope of internal audit activities. Thus, the charter prescribes the internal audit activity’s relationships with other units within the organisation and with those outside.</p> <p>Option 1 is incorrect. Policies and procedures guide the internal auditors in their consistent compliance with the IAA’s standards of performance.</p> <p>Option 2 is incorrect. The IAA’s authority is defined in a charter approved by the board.</p> <p>Option 3 is incorrect. The purpose of the Code of Ethics is to promote an ethical culture in the profession of internal auditing.</p>		

Question	Correct answer	Study guide reference
1.11	1	Learning unit 5
<p>Option 1 is correct. Internal auditors must develop and document a plan for each engagement, including the engagement's objectives scope, timing, and resource allocations.</p> <p>Option 2 is incorrect. Whether the planned work will actually be completed on time cannot be known in the planning phase.</p> <p>Option 3 is incorrect. Observations are what is actually found by performing procedures. Auditors must not anticipate the results of the work. To do so indicates a lack of objectivity.</p> <p>Option 4 is incorrect. Documenting the economic and efficient use of resources can be done only on completion of the engagement.</p>		
Question	Correct answer	Study guide reference
1.12	3	Learning unit 6
<p>Option 3 is correct. Internal auditors must develop and document a plan for each engagement, including the engagement's objectives, scope, timing, and resource allocations. Identifying sufficient information to achieve engagement objectives is done during field work, not planning.</p> <p>Option 1 is incorrect. The planning process includes obtaining background information.</p> <p>Option 2 is incorrect. The planning process includes obtaining background information.</p> <p>Option 4 is incorrect. The planning process includes determining how, when, and to whom the engagement results will be communicated.</p>		
Question	Correct answer	Study guide reference
1.13	2	Learning unit 2
<p>Option 2 is correct. Internal auditors should refrain from assessing specific operations for which they were previously responsible. Objectivity is presumed to be impaired if an internal auditor provides assurance services for an activity for which the internal auditor had responsibility within the previous year. Thus, if Francina provides assurance services for payroll, his objectivity is presumed to be impaired. Internal auditors may provide consulting services relating to operations for which they had previous responsibilities.</p> <p>Option 1 is incorrect because providing consulting services regarding payroll will not</p>		

impair the independence or objectivity of Francina.

Option 3 is incorrect because providing consulting services regarding payroll will not impair the independence or objectivity of Francina.

Option 4 is incorrect because providing assurance services regarding payroll will impair the objectivity of Francina.

Question	Correct answer	Study guide reference
1.14	2	Learning unit 4

Option 2 is correct. According to Sawyer's Internal Auditing (The IIA 1996, p. 4), an operational engagement involves a "comprehensive review of the varied functions within an enterprise to appraise the efficiency and economy of operations and the effectiveness with which those functions achieve their objectives."

Option 1 is incorrect. A financial engagement involves the analysis of the economic activity of an entity as measured and reported by accounting methods.

Option 3 is incorrect. A compliance engagement is a review of both financial and operating controls and transactions to determine conformity with established standards. It tests adherence to management's policies, procedures, and plans designed to ensure certain actions.

Option 4 is incorrect. A full-scale engagement relating to the manufacturing operation has financial, compliance, and operational aspects. It exceeds the chief executive officer's request.

Question	Correct answer	Study guide reference
1.15	1	Learning unit 6.2

Option 1 is correct. Among the common factors used in risk models for establishing the priority of engagements is management competence. Hence the internal auditor could appropriately consider the extent of management competence, which includes judgment, as a risk factor.

Option 2 is incorrect. Risk analysis considers both the potential loss (or damages) and the probability of occurrence. An area with the largest potential loss may have a very low likelihood.

Option 3 is incorrect. A high probability of occurrence may be associated with a small potential loss.

Option 4 is incorrect. The concept of risk analysis is not limited to quantitative measures.

Question	Correct answer	Study guide reference
1.16	2	AUI2601
<p>Option 2 is correct. Verifying that the prompt feedback on variances is provided to management is one way internal auditors facilitate the management function of controlling.</p> <p>Option 1 is incorrect. This relates to the management function of organising.</p> <p>Option 3 is incorrect. This relates to the management function of directing.</p> <p>Option 4 is incorrect. This relates to the management function of planning.</p>		
Question	Correct answer	Study guide reference
1.17	2	Learning unit 6.1
<p>Option 2 is correct. Management has the responsibility of ensuring the timely implementation of the audit recommendations. The IAA is responsible for the development of a timely procedure to monitor the disposition of the audit recommendations. It works with senior management and the board to ensure that audit recommendations receive appropriate attention.</p> <p>Option 1 is incorrect. An IAA role is to support the board in enterprise-wide risk assessment. The board and management are responsible for the identification of an appropriate risk model and methodology.</p> <p>Option 3 is incorrect. The IAA should monitor compliance with the corporate code of conduct set by the board and management.</p> <p>Option 4 is incorrect. The IAA is responsible for discussing significant financial, technical, and operational risks and exposures as well as the plans to minimise such risks.</p>		
Question	Correct answer	Study guide reference
1.18	1	Learning unit 6.3
<p>Option 1 is correct. The purpose of control processes is to support the organisation in the management of risks and the achievement of its established and communicated objectives. The control processes are expected to ensure, among other things, that operations are performed efficiently and achieve established results.</p> <p>Option 2 is incorrect. Collusions is and inherent limitation of internal control.</p> <p>Option 3 is incorrect. The board provides oversight of risk management and control</p>		

processes administered by management.

Option 4 is incorrect. Controls are actions by management, the board, and others to manage risk and increase the likelihood that established goals and objectives will be achieved. The IAA evaluates the effectiveness of control processes. Thus, controls do not directly address management's planning, organising, and directing processes. Internal auditors evaluate management processes to determine whether reasonable assurance exists that objectives and goals will be achieved.

Question	Correct answer	Study guide reference
1.19	1	Learning unit 6.3

Option 1 is correct. Preventive controls are actions taken prior to the occurrence of transactions with the intent of stopping events with negative effects from occurring. Use of an approved vendor list is a control to prevent the use of unacceptable suppliers.
 Option 2 is incorrect. A detective control identifies errors after they have occurred.
 Option 3 is incorrect. Corrective controls correct the problems identified by detective controls.
 Option 4 is incorrect. Monitoring controls are designed to ensure the quality of the control system's performance over time.

Question	Correct answer	Study guide reference
1.20	4	Learning unit 5

Option 4 is correct. It is virtually impossible to audit effectively something that is not sufficiently understood. The success of any engagement ultimately depends largely on how well the internal audit team understands the auditee. The first thing the internal auditors must understand is the auditee's business objectives and assertions. The internal audit team also must identify and assess the business risks that threaten the achievement of the auditee's objectives, identify the controls that are most critical to reducing business risks to acceptably low levels, and determine whether the identified key controls are designed adequately to reduce risks, both individually and collectively, to acceptably low levels.
 Option 1 is incorrect. An attitude of professional scepticism should be maintained throughout the audit.
 Option 2 is incorrect. Constructive suggestions are reserved for the reporting phase of each audit.
 Option 3 is incorrect. These actions are taken during the execution and reporting phase of each audit.