**LAIKIPIA UNIVERSITY COLLEGE**

**Attempt Question ONE and choose TWO other questions**

1. Take the following case of university exams administration at the Laikipia University College

* The lecturer in charge sets a draft exam.
* The exam is handed over to the chair of the department for checking. If satisfied, the chair signs the draft exams, otherwise he/ she returns the draft to the lecturer for amendments.
* The draft exam is then forwarded to the external examiner who checks the exam. If satisfied, the external examiner signs the draft exam. If not satisfied, the exam may be referred back to the lecturer of the department for appropriate changes through the office of the chair.
* Exam draft is forwarded to the exams department for typesetting.
* The lecturer in charge checks the draft exams that have been typeset, noting any spelling mistakes and omissions. If satisfied that the exam is proper, he/she signs the exam as approved, otherwise he / she fills a separate form indicating corrections to be made by the exams department.
* Final exam draft is printed ready for administration.

1. A flow chart with appropriate notes for the process. (16 mks)
2. What are the advantages of flow charts (2.5 mks)

*(i) They portray the flow of documents through the system and enable the auditor to relate those movements with procedures and checks carried out as part of that system.*

*(ii) They show the movement of documents in such a way that, when properly prepared, the sources and destinations of all documents will be clear.*

*(iii) They help to highlight weaknesses in the control of the business.*

*(iv) They enable audit tests to be clearly related to weaknesses in the accounting system.*

1. Discuss **narrative notes** as an alternative to the use of flow charts in documenting internal controls, highlighting the advantages and disadvantages. (5 mks)

*This is a simple and apparently convenient way of describing systems. Having ascertained the system, the*

*auditor draws up a narrative description of it for the audit files. An example might be: Sales invoices are prepared by Mr.\_\_\_\_\_ They are checked by Mr. \_\_\_\_\_ and then passed to Mr. \_\_\_\_\_ for recording in the customer’s account in the sales ledger etc.*

*Shortcomings of the method:*

*1. Notes can take up a disproportionate amount of space*

*2. Notes may be difficult to interpret*

*3. What happens it personnel change?*

1. Discuss in detail the following general principles of auditing

***Professional Ethics***

*There are a number of ethical matters that are extremely important for auditors to consider when performing their work. It is vital to the public image and credibility of the profession that the auditor is seen to be behaving in an acceptable manner in addition to actually complying with the ethical requirements.*

*It is important to recognize that many groups in society rely on accountant’s work, not just the shareholders on whose behalf the accountant is working. The accountant therefore has a public accountability. In the light of this, ICAP’s ethical guidelines emphasis the following key points about the characteristics of accountants:   
  
a)* ***Independence:***

*Auditor is independent of management i.e. he is not under the control or influence of management.*

*b)*  ***Integrity:***

*Auditor is honest and is not corrupt. He is straight forward in performing his professional work.*

*c)* ***Objectivity:***

*He obtains the evidence needed to form an opinion and his opinion is based on that evidence alone. He is not subjective in forming his opinion.*

*d)*  ***Professional Competence and Due Care:***

*Auditor has attained certain professional qualification, has acquired the requisite skill and has attained the experience necessary for the audit and performs his work with planning and due diligence.*

*e)*  ***Confidentiality:***

*Auditor neither discloses the information obtained during the course of his audit without permission of his client (except when required in a court of law) nor uses that information himself.*

*f)* ***Professional Behavior:***

*He should not only act in a professional manner but should also appear to be a professional. He should maintain his professional knowledge and skill at a level required to ensure that a client or employer receives the benefit of competent professional service based on up-to-date developments in auditing practice and relevant legislation.*

*g)*  ***Technical Standards:***

*Audit should be performed by following certain standards, international or national.****International Standards on Auditing (ISAs)***

*The auditor should follow basic principles and essential procedures together with related guidance as contained in ISAs. International Standards on Auditing (ISAs) are issued by the International Auditing Practices Committee (IAPC). The IAPC is a standing committee of the Council of the International Federation of Accountants (IFAC), which was formed in 1977 and is based in New York. IFAC has more than 150 member bodies, representing over 2 million accountants in more than 100 countries, and membership of IFAC automatically confers.*

*The IAPC issued standards and statements on auditing and related services in order to improve the   
degree of uniformity of auditing practice and related services throughout the world. The IAPC works closely with its members and national standard setters in order to gain acceptance of international Standards of Auditing (ISAs). Member bodies have increasingly sought to align the national position with the international positions IFAC and the IASC have gained influence and recognition. Standard setters increasingly refer to the international position in their consultative documents as authoritative support for a particular view.*

*International auditing and accounting standards do not at present override local regulations. Neither IFAC nor the IASC can currently compel any organization to comply with international standards; nor are there specific sanctions where organizations claim to have complied with international standards, but have not done so.*

*The preface to International Standards on Auditing and Related Services (ISA 100) states that IAPC guidance   
falls into two categories:*

***International Standards on Auditing (ISAs)*** *ISAs contain basic principles and essential procedures, together with related guidance in the form of explanatory and other material.  
   
The basic principles and essential procedures are to be understood and applied in the context of explanatory and other material that provides guidance for their application. The text of a whole standard is considered in order to understand and apply the basic principles and essential procedures.*

***International Auditing Practice Statements (IAPSs).***

*In conducting an audit in accordance with ISAs, the auditor is also aware of and considers International Auditing Practice Statements (IAPSs) applicable to the audit engagement. IAPSs provide practical assistance to auditors in implementing standards and promote good practice. They are not intended to have the authority of standards.   
The auditor may also conduct the audit in accordance with both ISAs and auditing standards of a specific jurisdiction or country.*

***Professional Skepticism***

*The audit should be planned and performed with an attitude of professional skepticism i.e. forming an opinion only after obtaining sufficient and appropriate audit evidence instead of blindly accepting any information or explanation given by the management. An attitude of professional skepticism means the auditor makes a critical assessment, with a questioning mind, of the validity of audit evidence obtained and is alert to audit evidence that   
contradicts or brings into question the reliability of documents and responses to inquiries and other information obtained from management and those charged with governance.*

1. The scope of internal auditing is found in the Institute of Internal Auditors’ Implementation Standards.
   1. Describe the scope of the internal audit function (12 mks)

***Reliability and integrity of financial and operational information*** *Internal auditors review the reliability and integrity of financial and operating information and the means used to identify, measure, classify and report such information.*

***Effectiveness and efficiency of operations*** *Internal auditors should appraise the economy and efficiency with which resources are employed. They should also review operations or programmes to ascertain whether results are consistent with established objectives and goals and whether the operations are being carried out as planned.*

***Safeguarding of assets*** *Internal auditors should review the means of safeguarding and, as appropriate, verifying the existence of such assets.*

***Compliance with laws, regulations and contracts*** *Internal auditors should review the systems established to ensure compliance with those policies, plans, procedures, laws, regulations and important contracts that could have a significant impact on operations and reports, and should determine whether the organization is in compliance.*

* 1. What are the implications of the wide scope of internal audit function with specific reference to

*The scope of internal auditing defined above is wide and this has several implications:*

***a. Expertise*** *Great expertise is required from auditors to enable them to provide advice on the wide range of key control objectives.*

***b. Safeguarding assets*** *It is necessary to establish who is responsible for investigating fraud since this is resource-intensive.*

***c. The compliance role*** *Controls over compliance may include an inspection routine and audit’s role in this should be clearly defined.*

***d. Information systems*** *The audit of management information systems (MIS) is crucial since this may involve reviewing MIS as part of operational audits, or these systems can be audited separately.*

***e. Value for money*** *The concept of economy, efficiency and effectiveness (or VFM) is another sensitive issue. Auditors can assist management’s task in securing good arrangements for promoting VFM or alternatively undertake a continual search for waste and other poor VFM.*

***F, Management needs*** *A wide scope requires a good understanding of the operations being reviewed and it is necessary to include management’s needs in the terms of reference by adopting a more participative style.*

***g. Specialists*** *The four elements of the key control objectives may require specialists in each of the defined areas and the level of expectation may place great demands on the audit service.*

1. Discuss the composition and the role of the audit committee, and explain the linkage between the audit committee and the internal and external audit functions (23.5 mks)

*The audit committee (AC) is a standing committee of the main board and tends to consist of a minimum of three non-executive directors (NEDs). Most audit committees meet quarterly and they are now found in all business and government sectors for larger organizations. The format is normally that the NEDs sit on the audit committee and the CFO, external audit, and CEO attend whenever required. The committee will have delegated authority to act in accordance with its set terms of reference and also investigate areas that again fit with their agenda.*

***The Role of the Audit Committee***

*An audit committee will be established by the main board to perform those duties that the board decides should be properly allocated to this specialist forum. The role of the audit committee may therefore incorporate some the following components in its terms of reference.*

1. ***The external audit process****- To review the external audit process and make recommendations to the board where appropriate.*

*2. The final accounts- To consider the annual accounts and the external audit report that attached to these accounts.*

*3.* ***Systems of internal control****- To consider the adequacy of systems of internal controls. The current move to require directors to report on their systems of internal control means that this is starting to assume a higher profile.*

*4.* ***Internal audit*** *Involvement in the appointment of the internal auditors and ensuring that the internal audit function operates to professional standards and performs well and discharges its responsibilities under the audit plan and strategy.*

*5.* ***Risk management-*** *The audit committee will ensure that there is an effective system of risk management within the organization and that this system supports the controls which, in turn, provide a reasonable expectation of achieving organizational objectives.*

*6.* ***Compliance and propriety****- An oversight of systems and procedures is in place to ensure compliance with regulations, policies, laws and procedures and the organization’s code of conduct. Also ensure that the organization is able to prevent, detect and respond to fraud and allegations of fraud.*

1. ***Financial management-*** *To consider the finances and expenditure of the organization and ensure that there is a good financial reporting and budgeting system in place and that this feeds properly into the process for preparing the annual accounts.*
2. *Special investigations- The audit committee may request special investigation from the internal audit, compliance officer, external auditor and external specialists where there is a need to probe into sensitive problems that fall within its remit.*
3. Discuss in detail the internal controls over wages and salaries, highlighting on the following specific areas

***(a) Approval and control of documents***

*i) There should be written authorization to employ or dismiss any employee.*

*ii) Changes in rates of pay should be authorized in writing by an official outside the wages department.*

*iii) Overtime worked should be authorized in advance by a manager/supervisor,*

*iv) An independent official should review the payroll and sign it.*

*v) The wages cheque should be signed by two signatories and agreed with the signed payroll.*

*vi) Where weekly pay relates to hours at work, clock cards should be used. There should be supervision of the cards and the timing devices, particularly when employees are clocking-on or off.*

*vii) Where a piece work system operates, payment should only be made for work of an appropriate quality which has been inspected and approved.*

*viii) Personnel records should be kept independently of the payroll department for each employee giving details of engagement, retirement, dismissal or resignation, rates of pay, holidays etc, with a specimen signature of the employee.*

*ix) A wages supervisor should be appointed who could perform some of the authorization duties listed above.*

***(b) Arithmetical accuracy***

*(i) Where appropriate, payroll should be prepared from clock cards, job cards etc, and a sample checked for accuracy against current 'rates of pay.*

*(ii) Payroll details should be checked for '.he accurate calculation of deductions e.g. tax, social security, pensions, trade union subscriptions etc*

***(c) Control accounts***

*(i) Control accounts should be maintained in respect of each of the deductions showing amounts paid periodically to the inland Revenue, trade unions etc.*

*(ii) Overall analytical checks should be carried out to highlight major discrepancies e.g. check against budgets, changes in amounts paid over a period of time, check against personnel records.*

*(iii) Management should exercise overall review and control.*