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| **Client name** | : | Cosmopolitan Industries (Pvt.) Limited | | | |
| **Accounting Period** | : | 01 July 2021 to 30 June 2022 | | | |
| **Subject** | : | Memo on Journal Entry Testing | | | |
| **Prepared by** | : | Imtiaz Rashid | **Date** | : | 05 Nov 2022 |
| **Reviewed by** | : | Salauddin Morshed | **Date** | : | 10 Nov 2022 |
| **Further Reviewed by** | : | Faruk Uddin Ahammed, FCA, CISA | **Date** | : | 15 Nov 2022 |
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**Background:**

The MEMO aims to document our conclusions regarding the audit procedures performed for testing journal entries for management override of controls in accordance with *International Standard on Auditing (ISA) 240* *The Auditor`s Responsibilities Relating to Fraud in an Audit of Financial Statements*, *Consideration of Fraud in a Financial Statement Audit*, for Statutory Audit of Cosmopolitan Industries (Pvt.) Limited for the year ended 30 June 2022. In preparing this memo, we have reviewed and considered the Deloitte Guide to Journal Entry Testing to Address the Risk of Management Override of Controls (“Deloitte JE Guide”).

**Scope of Audit:**

Local Statutory Audit – Year ended 30 June 2022.

**Reference to International Standards on Auditing (ISA):**

ISA 240, effectively we need to cover 3 aspects for MOC:

Irrespective of the auditor’s assessment of the risks of management override of controls, the auditor shall design and perform audit procedures to:

**(a)** **Test the appropriateness of journal entries**

**(b)** **Review accounting estimates for biases**

**(c)** **Significant transactions that are outside the normal course of business**

To perform **Significant transactions that are outside the normal course of business,** Engagement Team (ET) has followed the following procedure:

**Test for Unusual Transactions:**

1. Engagement Team (ET) has performed the JE profiling to identify the unusual entries and obtained appropriate business rationale for those entries. ET has used spotlight to perform JE profiling supported by Group Auditor.

Firstly, ET has performed integrity testing for the whole year. ET has tried to combine the full data dump into one single file. There were 272,550-line items in the full Data Dump. Refer to **Data dump-CIPL- June 2022.**

**Step 1:** ET has extracted the manual journal entries from the data dump. Then inserted the manual journal entries to the **Population** tab of the Spotlight Solutions for analysis.

**Step 2**: Then, ET conducted an integrity test. No difference was found between TB movement and JE Dump movement. We. Refer to **WP#FSL.P01.1 Profiling of Journal entry testing.**

**Step 3**: The ET performed tailoring based on 14 profiling criteria, and finally performed JE testing based on 14 profiling criteria. Procedures followed in this regard are as follows.

1. **Entries Made to** **Unusual Accounts:** ET performed a detail review of list of accounts, including the account descriptions, and did not identify any account descriptions that we believed to be unusual, unique, or inconsistent with the type of accounts the Company would have. We also reviewed the account numbers and number of entries posted to each account to identify accounts that could be unusual as a result of the account number or the activity in the account. We have identified some keywords to ensure whether any unusual accounts exist such as **fraud, temporary, bonus, unknown, gift, government officials, bribe, Adjustment** etc. To identify the relevant account for this exception, we have used spotlight. Spotlight has found 20 exceptions under these criteria. We have analyzed the exception items and discussed with Management to understand the nature of transactions and their business rationale. Based on our understanding and discussion with Management, we scoped out 10 items and selected 10 items for substantive testing. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
2. **Entries Made to Seldom Used Accounts:** The significance of the parameter was to identify all accounts number along with entries where less than 5 entries were posted on those accounts during the period. Spotlight has found 36 exception items for which justifications are noted based on inquiry with management. We have analyzed the exception items and discussed with Management to understand the nature of transactions and their business rationale. Based on our understanding and discussion with Management, we scoped out 33 items and selected 3 items for substantive testing. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
3. **Large Debits to Revenue During the Period:** We have selected debits made to the revenue during the period to test the appropriateness. We have discussed with the management and obtained understanding that it is usual to post debit entries in revenue such as when unbilled revenue is reversed (after month end). Upon further reviewing the revenue entries, we have determined a large amount which to be debited to revenue within 7 days of period end. To identify the relevant account for this exception, we have used Spotlight. No exception were found. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
4. **Users with Few Postings:** Users with few entriesgive suspicion and needs to be considered as audit interest. This test identifies users who posted less than 2 entries during the month. No exception was identified. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
5. **Users of Interest:** We have inquired management to identify users of interest. This test Identifies journals based on the user ID (EGMFIN03, EGMFIN01) of the user who entered it. Spotlight has not found any exceptional entry. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in.**
6. **Entries Posted on weekends and holidays:** Due to home office and Covid situation most of the weekend finance team of the client office was doing work specially at the month. We have analyzed most of the transactions and did not notice any unusual transactions recorded on those weekend transactions.

From our assessment, we found that the transaction is reasonable, these have been incurred for the normal course of business and did not find any management override on the transactions. Hence, we have not selected for testing.

1. **Entries with Round Amounts:** The company regularly process amounts for round numbers and so this always could not be indicative of a potentially inappropriate entry by management. This is usual for this entity to have abundant transactions in round amounts. Based on our inquiry with the management, we have considered amounts with more than 7 rounding digits for our testing. Spotlight has found 46 entries under this exception. We have analyzed the exception items and discussed with Management to understand the nature of transactions and their business rationale. Based on our understanding and discussion with Management, we scoped out 44 items and selected 2 items for substantive testing. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
2. **Entries with Recurring Ending Digits:** The Company may process amounts for recurring ending digits, for example, while calculating the revenue or expenses, it is usual to have several decimal places as recurring digits, so this always could not be indicative of a potentially inappropriate entry by management. Therefore, large entries with recurring ending digits may be unusual. We have considered 5 Digit recurring which have occurred into the JE Dump. No exception were identified. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
3. **Largest journal lines:** This test may give us entries which is unusually large and relates to fraudulent entries. For this reason, we have considered the entries made with top X largest values (X is Performance materiality amount: USD 976,500). To identify the relevant entry for this exception, Spotlight has found 45 entries under this exception. We have analyzed the exception items and discussed with Management to understand the nature of transactions and their business rationale. Based on our understanding and discussion with Management, we scoped out 42 items and selected 3 items for substantive testing. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
4. **Entries Containing Keywords in Journal Entry and/or Journal Line Description:** The test is selected to find out such keywords in the entry such as **Bribe, Gift, Present, Government officials, Satisfy, Adjustment, Reimbursement, help, reverse, restate, fraud, Error** etc. which may indicate fraudulent entries. These words selected are based on our understanding of common fraud-related activities and inquiry with management personnel. To identify relevant entries for this exception, we have used the built-in formulas. Spotlight has found 11 entries under this exception. We have analyzed the exception items and discussed with Management to understand the nature of transactions and their business rationale. Based on our understanding and discussion with Management, we scoped out 9 items and selected 2 items for substantive testing. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
5. **Pre posted and back posted entries:** The test is relevant as it will give entries those have posting date and effective date 7 days difference. To identify relevant entries for this exception, we have used Spotlight. Here, Spotlight has not found any entry according to our set criteria for this exception. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
6. **Unrelated Accounts:** Entries in unrelated accounts imply that any unnatural or fraudulent entries through which management may try to conceal. Based on our knowledge of the Financial Reporting Process of the company, the prior test results, current year’s analytical procedure test result, and review of Journal Dump, possibility of entries recorded by the company does not involve unrelated accounts is very minimal. Accordingly, using spotlight we have not found any exception under these criteria. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
7. **Large PnL debit entries posted around year end:** This test gives us selections which unusually not like to occur with the nature of the transactions. So, for the entries made by unusual large debit to P&L items at the period end may indicate fraud risk. We have considered debit entry recorded above PM amount of 976,500 within 7 days of period end. To identify the relevant account for this exception, we have used Spotlight. Spotlight has found 6 exceptions here. We have analyzed the exception items and discussed with Management to understand the nature of transactions and their business rationale. Based on our understanding and discussion with Management, we have scoped out 5 item and selected 1 items for substantive testing. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
8. **Large PnL credit entries posted around year end:** This test gives us selections which unusually not like to occur with the nature of the transactions. So, for the entries made by unusual large debit to P&L items at the period end may indicate fraud risk. We have considered credit entry recorded above PM amount of 976,500 within 7 days of period end. To identify the relevant account for this exception, we have used Spotlight. Spotlight has found 4 exceptions here. We have analyzed the exception items and discussed with Management to understand the nature of transactions and their business rationale. Based on our understanding and discussion with Management, we have scoped out 3 item and selected 1 item for substantive testing. Refer to **WP FSL.P01.2 Justification of scoped out and scoped in**.
9. ET has performed Test of Details on the scoped-in items which were scoped in as unusual journal entries.
10. **Entries Made to Seldom Used Accounts:** In substantive testing of 3 scoped-in items, we reviewed the supporting document and found that the transactions were incurred for business purposes and concluded that no fraud characteristic exists in the transactions. Refer to **WP FSL.P01.3 TOD on Journal entries**.
11. **Entries Made to Unusual Accounts:** In substantive testing of 10 scoped-in items, we reviewed the supporting document and found that the transactions were incurred for business purposes and concluded that no fraud characteristic exists in the transactions. Refer to **WP FSL.P01.3 TOD on Journal entries**.
12. **Entries with Round Amounts:** In substantive testing of 2 scoped-in items, we reviewed the supporting document and found that the transactions were incurred for business purposes and concluded that no fraud characteristic exists in the transactions. Refer to **WP FSL.P01.3 TOD on Journal entries**.
13. **Entries Containing Keywords in Journal Entry and/or Journal Line Description:** In substantive testing of 2 scoped-in items, we reviewed the supporting document and found that the transactions were incurred for business purposes and concluded that no fraud characteristic exists in the transactions. Refer to **WP FSL.P01.3 TOD on Journal entries**.
14. **Largest journal lines:** In substantive testing of 3 scoped-in items, we reviewed the supporting document and found that the transactions were incurred as normal courses of business and concluded that no fraud characteristic exists in the transactions. Refer to **WP FSL.P01.3 TOD on Journal entries**.
15. **Large PnL debit entries posted around year end:** In substantive testing of 1 scoped-in item, we reviewed the supporting document and found that the transactions were incurred as normal courses of business and concluded that no fraud characteristic exists in the transactions. Refer to **WP FSL.P01.3 TOD on Journal entries**.
16. **Large PnL credit entries posted around year end:** In substantive testing of 1 scoped-in items, we reviewed the supporting document and found that the transactions were incurred as normal courses of business and concluded that no fraud characteristic exists in the transactions. Refer to **WP FSL.P01.3 TOD on Journal entries**.

**Overall Conclusion:**

Based on the results of the testing performed above, it may be concluded that ET has been able to address the Risk of Management Override of Control as Significant Risk.

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