

Internal Audit Evidence, Documentation & Sampling

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- Inter-relationship of Evidence, Documentation & Sampling
- Audit evidence
- Documentation
- Sampling

How do they co-relate...

- **Define audit universe**

- **Risk assessment**

- Long term audit plan

- Annual audit plan & Changes

- Approval from Audit Committee

- Initial data gathering

- **Pre-audit risk assessment**

- **Finalise data population and perform sampling**

- Audit plan & assign resources

- **Perform audit tests**

- Identify exceptions

- Evaluate results

- **Gather evidence**

- Discussion with auditee

- **Closing meeting**

- Draft report

- Validation of responses

- Final report

- Communicate with Audit Committee

- **Perform follow up audit**

- Report effective closure of audit observations

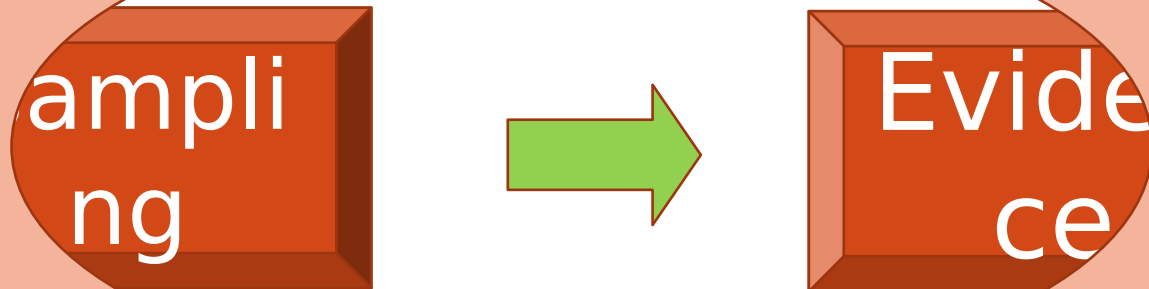
- Communicate with Audit Committee

Evidence Sampling

Need to Document

How do they co-relate...

Documentation



Evidence – let's understand it deeper..

- Professional requirements
 - SIA 10 of ICAI requiring an auditor to obtain sufficient appropriate evidence to enable him to draw reasonable conclusions therefrom on which to base his opinion or findings.
 - IIA specified Performance standard 2310 on identifying information and mentions that the Internal auditors must identify sufficient, reliable, relevant, and useful information to achieve the engagement's objectives.
- Risk assessment determines the degree of sufficiency and appropriateness of the audit evidence to be obtained.. The quantity of audit evidence needed is affected by the risk of misstatement (the greater the risk, the more audit evidence is likely to be required) and also by the quality of such audit

Evidence – let's understand it deeper..

- **Higher the Appropriateness, lower sufficiency will be necessary, but reverse is not true**
- **Level of evidence increases with sensitivity of the assignment**

Time & cost of obtaining evidence

- Higher time and cost required to be spent in obtaining evidence may directly affect the performance of audit
- Higher time & cost may improve the effectiveness but hamper the efficiency

Reliability of audit evidence

- Audit evidence from external sources is more reliable than that obtained from Entity's records
- Evidence from Entity's records is more reliable when internal controls work effectively
- Direct evidence by auditors is more reliable than obtained from the Entity
- Written evidence is more reliable than oral

● Original documents are more reliable than photocopies

Though the above rules are generally true, care must be taken to co-relate the same with the nature of assignment and objectives of the assignment

Evidence obtained through...

Traditional Vs Current - eVIDENCE

Concepts don't change over time but the underlying procedures change drastically.. Innovations, automation and speed are the key changes

eVidence

- Understanding the client's ERP system - organisational setups, reporting modules, authorisation, independence
- Ascertaining completeness
- Direct from ERP or converted to Excel
- Ability to operate Client's ERP system
- Protecting date & time stamps of soft files, emails, etc
- Protecting the evidence through timely back ups on a standalone drives, controlling access & modification rights
- In case of high end investigations, protect the evidence from electromagnetic interferences

Simple review of date & time stamp – MS

V0 Purchase Orders Properties

General Security Details Previous Versions

V0 Purchase Orders

Type of file: Microsoft Excel Worksheet (.xlsx)

Opens with: Microsoft Excel Change...

Location: C:\Users\nlikhite\Downloads

Size: 10.7 MB (11,243,647 bytes)

Size on disk: 10.7 MB (11,247,616 bytes)

Created: Today, August 21, 2016, 1 minute ago

Modified: Today, August 21, 2016, 8:40:24 AM

Accessed: Today, August 21, 2016, 1 minute ago

Attributes: Read-only Hidden Advanced...

Security: This file came from another computer and might be blocked to help protect this computer. Unblock

V0 Purchase Orders Properties

General Security Details Previous Versions

Property	Value
Description	
Title	
Subject	
Tags	
Categories	
Comments	
Origin	
Authors	sapatil
Last saved by	pchattop
Revision number	
Version number	
Program name	Microsoft Excel
Company	
Manager	
Content created	8/17/2016 9:46 AM
Date last saved	8/19/2016 5:01 PM
Last printed	
Content	

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Offline availability	
Offline status	
Shared with	
Computer	ACC-THANE-L263 (this computer)

[Remove Properties and Personal Information](#)

Some key evidences (other than audit execution)

- Minutes of meeting (MOM)
 - MOM of discussion and finalisation of audit plans, scope restrictions
 - MOM of audit opening, discussions and closing meetings
- Audit responses
 - Circulation of queries for responses
 - Circulation of draft and final reports
 - Receipt of responses on draft reports

Emails with receipt acknowledgements are stronger than circulation of hard copies

Documentation

Audit Documentation

- SIA 2 by ICAI requires that The internal auditor should document matters, which are important in providing evidence that the audit was carried out in accordance with the Standards on Internal Audit and support his findings or the report submitted by him. auditor
- SIA 3 by ICAI on Documentation means “Internal audit documentation” means the record of audit procedures performed, including audit planning as discussed in the Standard on Internal Audit (SIA) 1, Planning an Internal

**Audit relevant audit evidence obtained and conclusions
Documentation refers to the entire audit process from plan to report and not restricted to audit execution working papers**

Audit Documentation enables us with visible benefits

- Assisting the engagement team to plan and perform the audit
- Provide evidence of the internal audit work performed to support the internal auditor's findings and opinion
- Assisting members of the engagement team responsible for supervision to direct and supervise the audit work
- Enabling the engagement team to be accountable for its work
- Provide evidence of the fact that the internal audit was performed in accordance with the scope of work as mentioned in the engagement letter
- Retaining a record of matters of continuing significance to

IA Documentation

IA Department Level

- Audit Committee Charter
- Internal Audit Charter
- IA Organisation

Company or client level

- Company organisation, locations, functions and management structure
- Delegation of authority

- Manufacturing process
- **The permanent documents should be reviewed once a year and updated for any changes in the organisational level**
- Internal control system/process guides including

Segregation of Duties

IA Documentation

- Audit universe
- Risk assessment results
- Long term /annual audit plan & changes
- Scope restrictions
- Agreement with management

- Audit engagement letter
- Understanding of the function and procedures under audit assignment
- Data analysis
- Risk assessment
- Audit plan & assign resources &

- Audit working papers such as contracts, approval notes, minutes, communications, etc
- Results of work performed and identification of exceptions
- Quantification of impact

- Closing meeting & MOM
- Draft report
- Receipt of audit responses
- Final report
- Communicate with Audit Committee
- Updation of audit

- Transactions selected for FU audit
- Documentation of audit procedures
- Communication of results
- Agreement with Auditee
- Final report
- Communicate with Audit

Audit Management & tracking Softwares

- Application to manage the entire audit lifecycle
- Provides standard templates of documentation, draft & final reports, monitors the audit execution
- Most of the 'on the shelf' products contain standard audit questionnaires / check lists
- Provides a central repository for maintenance of audit documentation
- Ensures standardisation in WP formats and contents
- Auto referencing is achieved
- Provides a review and signoff functionality
- Ability to send email alerts to the auditees on open audit

Documentation in Special audits

- Special audits e.g investigations require special emphasis on documentation
- Objective & agreed scope, scope restrictions, responsibilities of both parties to be documented clearly in an engagement letter or letter of agreement
- Data can be of diverse types, (audio visuals, testimonies, computer images, etc)
- Source and timings of documentation to be documented
- Controlled access to documentation
- Consultation of corporate legal teams in maintaining the evidence so that they could be used for litigations, police referrals, etc in times of need

Sampling

Sampling definitions

- IIA's practice advisory 2320-3 defines Audit sampling as, the application of audit procedures to less than 100 percent of items within a class of transactions or account balance such that all sampling units have a chance of selection.
- SIA 5 of ICAI defines audit sampling as the application of audit procedures to less than 100% of the items within an account balance or class of transactions to enable the internal auditor to obtain and evaluate audit evidence about some characteristic of the items selected in order to form a conclusion concerning the population.

Sampling is one of the techniques to gather sufficient and appropriate audit evidence.

- Requirement is to do 100% audit or data size is small to cover

Why sampling

- Size of organisations having huge volume of transactions
- Requirement to obtain sufficient, reliable, relevant and useful audit evidence
- Responsibility to give reasonable assurance
- Timing and resource constraints for completing the audit
- **CAATs and Data Analytics tools have made it possible to review 100% of the transactions or entire population**
- Have a focused attention for indepth reviews on few select (but representative) transactions rather than

Audit Sampling - determinants

- Objective of the audit assignments is the key to determine sampling, sampling method, sample size, etc
- Audit department should have a sampling policy in place so that it is applied consistently and understood by the auditees
- Defining and ascertaining completeness & relevancy of population determines the accuracy of sampling
- Statistical sampling deployment may require technical skills, availability of softwares and training
- SIA 5 specifically excludes selection of transactions having same particular characteristic as audit sampling
- Stratification of population will help in reducing the sample

Process to determine the sample

- State the objectives of audit assignment
- Decide whether sampling technique is desirable
- Define attributes and exception conditions
- Define the population
- Define sampling unit
- Specify tolerable exception rate
- Specify acceptable risk of assessing control risks too low
- Estimate population exception rate
- Determine initial sample size

Audit Sampling - determinants

- Assessment of risks is the key to sampling, we use:
 - Past audit experience, reports
 - Knowledge of industry, business, environment, legal framework, key changes
 - Nature of assignment (usual audit, investigation, etc)
 - Knowledge of the function
 - Company's internal control systems and its adequacy
- In all cases, we need to determine:
 - Risk of material misstatement
 - Sampling risk (for TOC & TOD)
 - Tolerable error

Sampling methods

- Statistical sampling – applying the statistical models to obtain a representative sample from the defined population
 - Random sampling
 - Systematic sampling
 - Probability Proportional to Size sampling
 - Stratified sampling

- Non-statistical sampling

Whichever sampling method is used, consideration must be given to the assessment of material misstatements, sampling risk, assessment of tolerable error and expected error in the given population

More on Statistical sampling

Advantages:

- Deployment will result in reasonable assurance from review of limited no. of transactions
- Provides the measurable back up for sample selection
- Unbiased selection of sample
- Quantification of risks and materiality
- Once deployed, the consistency in the sampling is ensured across the

Shortcomings:

- Limited scope for judgement of the auditor coming from experience
- Require time and cost for imparting trainings
- Time required to be spent in explaining the output

More on Non-statistical sampling

Advantages:

- Uses the auditors judgement, flexibility and outside factors in selection of samples
- No costs involved
- Less rigid approach to unique problems

Shortcomings:

- Requires maintaining proper backups
- The basis of selection is not fixed and needs to be documented
- Lesser objectivity as factors such as sampling risk, audit risks, etc are not factored in

Attribute sampling and variable sampling

- Attribute sampling
 - Used for compliance testing (Yes/No)
 - For testing the effectiveness of controls (Test of Controls)
 - No. of times a particular characteristics may occur in a population

- Variable sampling
 - Used for substantive testing
 - For testing the correctness of monetary terms in terms of completeness, existence, accuracy, rights & obligations,

Correlation of sampling risk with efficiency & effectiveness

Audit test	Audit efficiency	Audit effectiveness
Test of controls	Risk of assessing control risk too high	Risk of assessing control risks too low
Test of details (Substantive tests)	Risk of incorrect rejection	Risk of incorrect acceptance

- **In both the above scenarios, the audit efficiency as well as audit effectiveness will be impacted.**
- **Pre-audit risk assessment and auditors judgement are required to determine use of sampling to balance audit effectiveness and efficiency**

Steps in sampling – Test of controls

- Define objectives of audit
- Decide whether audit sampling applies
- Define attributes and exception conditions
- Define Population
- Define sampling unit
- Specify Tolerable exception rate
- Specify Acceptable risk of assessing control risk too low
- Define Population exception rate
- Determine initial sample size

- Select the sample
- Perform the audit procedures

- Generalise from the sample to the population
- Analyse exceptions
- Decide acceptability of the population

Evaluation of sampling results

- Auditor to apply the same audit procedures on all samples selected and document the results
- After applying the decided audit procedures on few of the samples, evaluate the results with the objectives and have an early assessment of either relooking at the population and sample OR application of the required audit procedures
- The auditor to state the fact of use of sampling in the final report and results of the same
- Financial quantification should be done on entire population using proportion method to bring an impact to the observation

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*Thank
you*

