

Process flow diagrams and other documentation

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Topic 1: Audit lessons

Audit lessons

- Teams did not sufficiently understand the likely sources of potential misstatements related to significant accounts or disclosures as part of selecting controls to test.
 - Teams walkthrough procedures were not adequate to verify the auditor's understanding of the risks in the company's processes and to identify and select for testing controls sufficient to address the risk of misstatement for the relevant assertions as they were limited to:
 - Performing inquiry and observation to confirm that there have been no significant changes to the processes
 - Obtaining an understanding through controls testing and substantive procedures
 - Reviewing walkthroughs performed by the company's internal auditor who did not provide direct assistance under the firm's supervision
 - Relying on the auditor's knowledge and experience obtained from prior year's audits.
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Topic 2: Process flows



Process flows

- A process flow generally consists of:
 - Following a single transaction from origination through the entity's processes, including information systems, until it is reflected in the entity's financial records.
 - Using the same documents and information technology that entity personnel use.
 - Probing inquiries of the entity's personnel about their understanding of what is required by the entity's prescribed procedures and controls at the points at which important processing procedures occur.
 - Asking personnel to describe their understanding of the previous and succeeding accounting or control activities and to demonstrate what they do to corroborate information at various points in the walkthrough.
- Combination of inquiry, observation, and inspection

Key Points for Understanding the Process

- Cover from the initiation of the transaction to recording in the financial statement and understand all processing in between.
- Document and trace the flow of information, not controls.
- Document key points of information, whether in the client's narrative or on a flowchart.
- Walk through the IT system, not around it.
- Understand relevant data elements in the process.
- Involve experienced team members for complex areas.
- Don't get locked into prior year's documentation.

Walk through processes, not controls!

Obtaining an Understanding

Have you identified and documented:

- All relevant assertions associated with each significant account and disclosure?
- The flow of transactions related to each relevant assertion?
- The points within the process where a misstatement could arise that individually or in aggregate with other misstatements could be material?
- The controls that management has implemented to address potential misstatements?

It is important that engagement teams are able to answer these questions and that these answers are reflected in their documentation.

Walkthrough Documentation


- Location where the walkthrough occurred.
- Date(s) the walkthrough occurred.
- Audit firm interviewer.
- Client interviewee.
- Transaction(s) traced, including identifying characteristics of the transaction(s).
- Document(s) reviewed, including identifying characteristics of the document(s).
- Other Considerations
 - Probing follow-up question(s) that were asked by the audit firm interviewer(s) of the interviewee(s), and any notable responses.

Consider IT controls as you document your walkthroughs.

Key Attributes of Documentation Related to IT

Process Level Understanding

- Provides understanding of how ***specific data elements*** of interest are captured and flow through information system to financial statements.
 - Addresses ***manual and IT processes*** in a way that avoids process gaps in documentation.
 - Describes ***relevant activities within IT systems***, not just inputs and outputs.
 - Describes and ***differentiates IT system components*** to allow for identification of specific risks.
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Topic 3: Flowcharting

What is Flowcharting?

Flowcharting is used to visually represent client processes and accounting systems so we can more easily identify and document the WCGWs and assess the design of the controls over those WCGWs.

Flowcharting – Potential Advantages and Challenges

Advantages:

Simplification and clarification of documentation.

Easier to identify IT applications and relevant IT controls.

Easier to visualize gaps or missing key controls.

Challenges:

Requires clear guidance about what needs to be captured in flowcharting to avoid wasted effort and/or too detailed documentation.


Initial time investment involved.

Requires incremental training.



Flowcharting Tips

Identify the output of the system (e.g. General ledger account, report used by management as the basis of a high level management review control).




Begin the documentation with the output of the system, making this a more efficient approach.



Check that all appropriate information has been linked to the source documentation.



Use active voice in your flowchart processes (i.e. "The employee enters information into the system" versus "Information is entered into the system").



Draw the flowchart such that information flows top to bottom and from left to right.

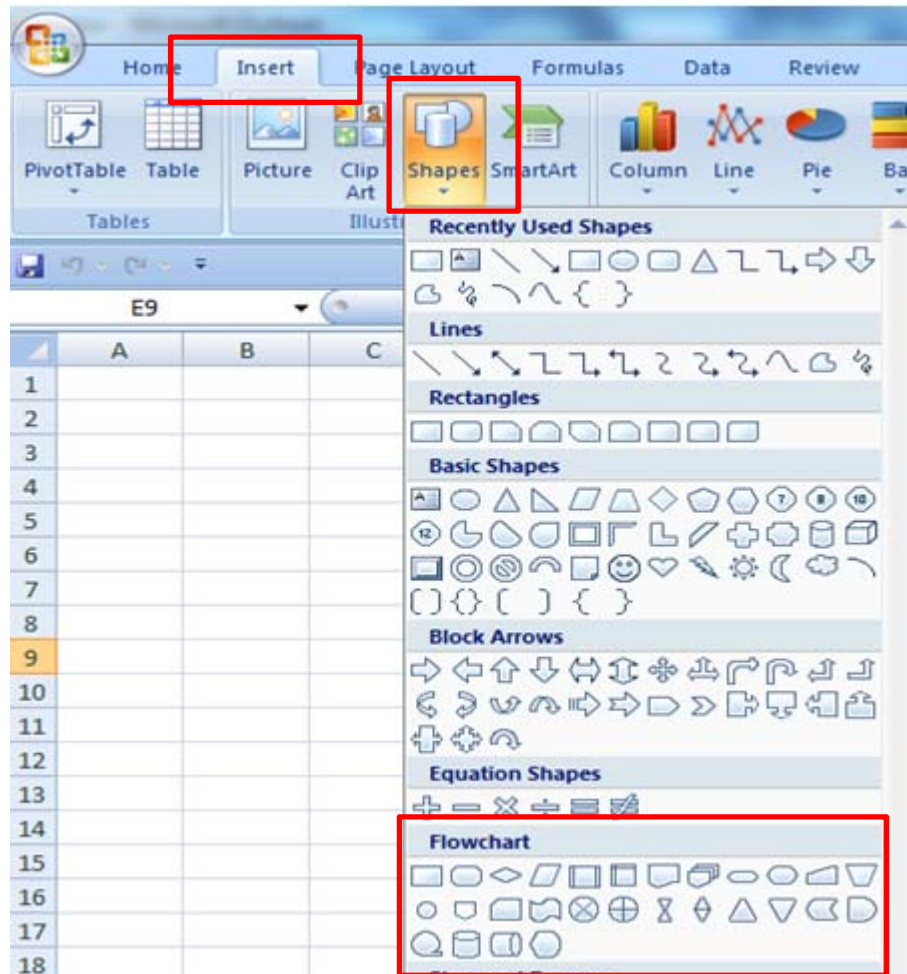
Flowcharting Considerations

When creating a process flow diagram, consider:

- Who are the individuals, departments, etc. involved in the process?
- How often is the process performed?
- What are the key activities in the process?
- In what order do the key activities occur?
- Where do the WCGWs reside in the process?
- Which relevant controls address the WCGWs?
- What are the various reports and data elements used in or generated from the process?
- Which systems are critical to the process?

Begin with the end in mind!

Flowcharting in Excel





**Topic 4:
Information produced
by entity**

Guidance Note has defined IPE

- The auditing standards do not provide a definition of information produced by the entity (IPE) or describe what constitutes IPE. IPE is typically in the form of a "report" which may be either system-generated, manually-prepared, or a combination of both (e.g., a download of system accumulated data that is then manipulated in an Excel spreadsheet).
 - Examples of different forms of reports include:
 - Standard "out of the box" or default reports or templates
 - Custom-developed reports that are not standard to the application and that are defined and generated by user-operated tools
 - Output from end-user applications such as automated spreadsheets
 - Entity-prepared analyses, schedules and spreadsheets that are manually prepared by entity personnel either from information generated from the entity's system or from other internal or external sources
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Understanding IPEs

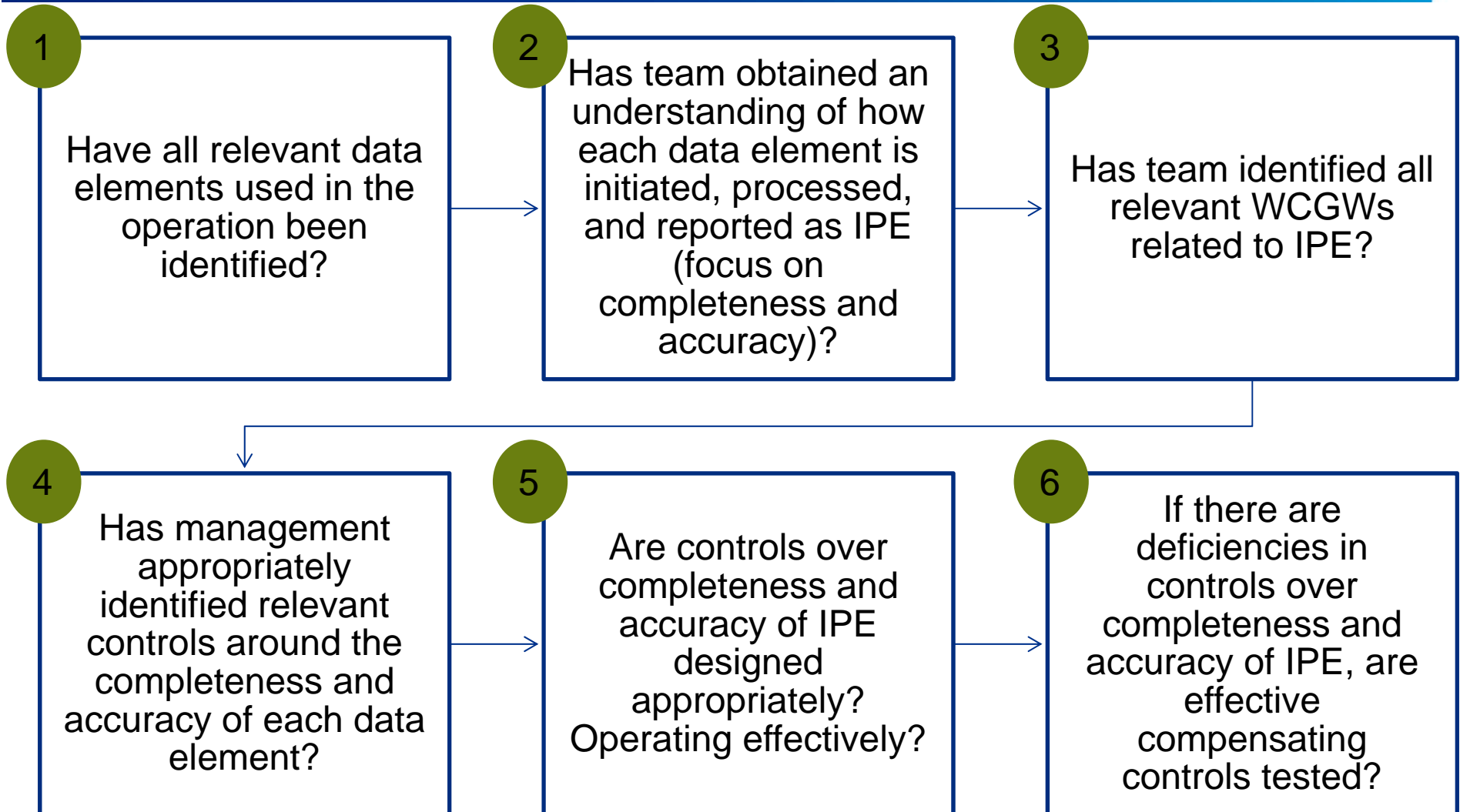
- IPE typically consists of three elements: (1) source data, (2) report logic, and (3) parameters.
 - **Source Data:** The information from which the IPE is created. This may include data maintained in the IT system (e.g., within an application system or database) or external to the system (e.g., data maintained in an Excel spreadsheet or manually maintained), which may or may not be subject to general IT controls. For example, for a report of all sales greater than Rs. 1,000,000, the source data is the database of all sales transactions.
 - **Report Logic:** The computer code, algorithms, or formulas for transforming, extracting or loading the relevant source data and creating the report. Report logic may include standardised report programs, user-operated tools (e.g., query tools and report writers) or Excel spreadsheets, which may or may not be subject to the general IT controls.
 - **Report Parameters:** Report parameters allow the user to look at only the information that is of interest to them. Common uses of report parameters including defining the report structure, specifying or filtering data used in a report or connecting related reports (data or output) together.
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Auditor considerations of IPE

- The following considerations related to accuracy and completeness of IPE may assist the auditor in obtaining an appropriate understanding to plan the testing approach to IPE:
 - Not all data is captured.
 - The data is input incorrectly.
 - The report logic is incorrect.
 - The report logic or source data could be changed inappropriately or without authorisation.
 - The user-entered parameters entered are incorrect.

 - Evaluating IPEs: The auditor is required to "evaluate whether the IPE is sufficiently precise and detailed for purposes of the audit". If the IPE is not sufficiently precise or detailed for the purpose, it is likely that the auditor cannot use it as audit evidence; however, the auditor may work with the entity to determine if the original IPE can be modified by the entity to meet his or her needs or identify other audit evidence to achieve the intended purpose.
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Test Controls over the C&A of IPE Used in MRC



Testing Controls over IPE – Key Points

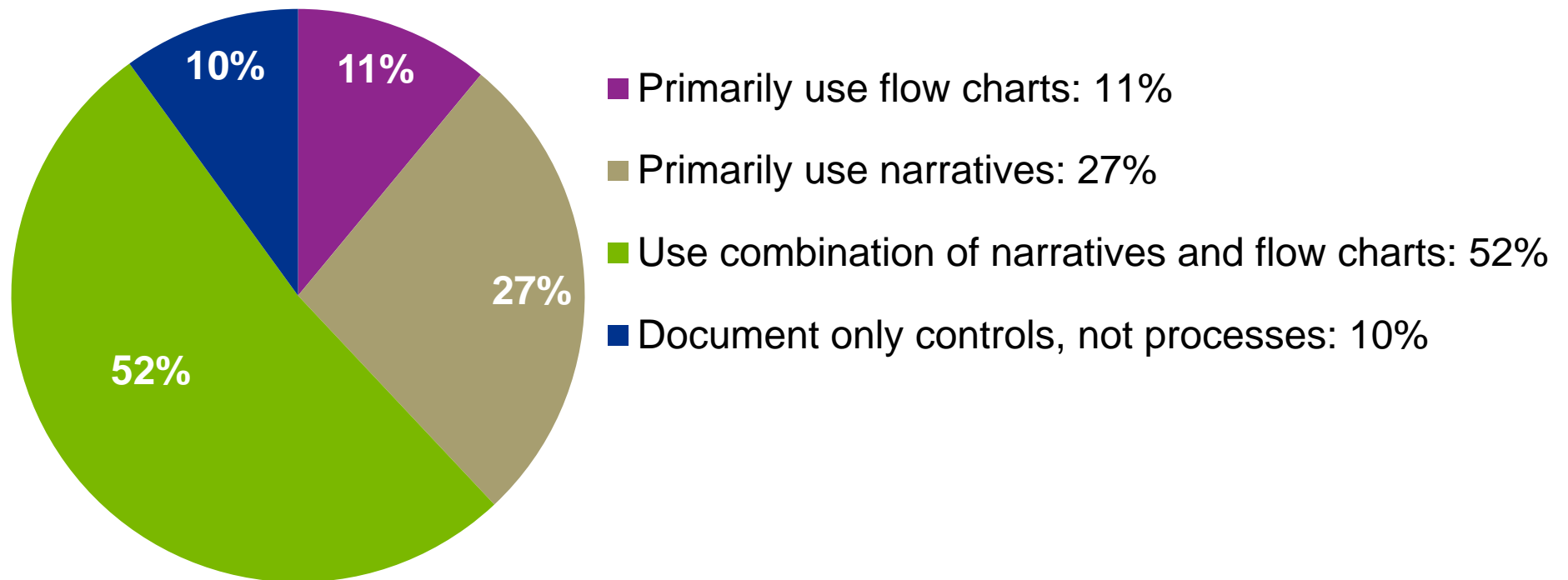
- Test the design and operating effectiveness of the controls over completeness and accuracy of IPE used in MRCs.
 - Determine the flow of each relevant data element, identify the related WCGWs and test the related controls.
 - Failure to have effective controls over completeness and accuracy of the IPE generally renders the MRC ineffective.
 - Ineffective GITCs generally render the MRC ineffective.
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Topic 5: Documentation

CFO Financial Forum Opinion Poll

Which of the following best describes your organization's documentation of business processes and controls?



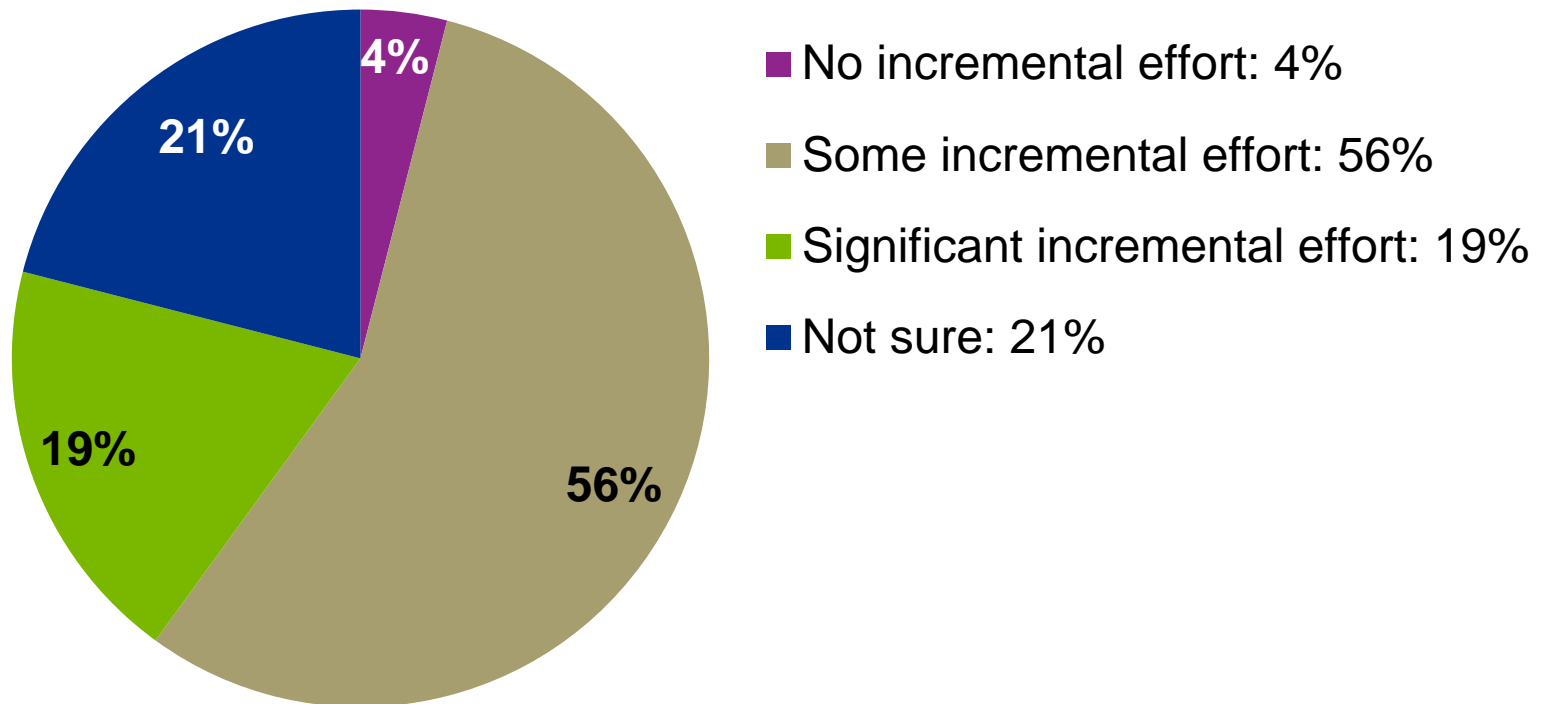
Ensure that management has documented in writing its control policies and procedures for all relevant business processes.

Documentation

- Effective documentation of the organization's system of internal control is necessary to:
 - Provide evidence of its effectiveness
 - Enable proper monitoring
- Effective documentation is also useful:
 - For assigning responsibility and accountability to employees
 - Training new and experienced employees who implement and monitor the controls
 - Promoting consistency across the organization
 - Retaining organizational knowledge
- Higher level of documentation necessary when management asserts effectiveness of internal controls to regulators, shareholders and other third-parties
 - Expanded documentation on design and operating effectiveness of controls
 - Expanded documentation in areas involving significant judgment

Documentation: CFO Financial Forum Opinion Poll

What additional effort is required to improve your documentation of ICOFR?



Documentation of existing and enhanced processes and controls is expected to be one of the main areas of additional effort when transitioning to IFCs

Thank you

