AWP 5.3

Understanding the Entity’s System of Internal Control

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| Name of the Entity | XYZ |
| Period of audit | 01.01.20XX to 31.12.20XX |

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| Evaluated by | | Signature | Reviewed & approved by | Signature |
| Name: |  |  |  |  |
| Designation: |  |  |
| Date: |  |  |

| **1** | **2** | **3** |
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| **Checklist** | **(Yes/No/NA)** | **If No, effect on assessment of ROMM** |
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|  |  | **Trace to AWP 5.4 – Table A** |
| 1. **CONTROL ENVIRONMENT** | | |
| **A. Structure and culture** |  |  |
| 1. Is there a clearly defined senior management structure? e.g ministry-level committee, senior management committee, executive committee, etc. |  |  |
| 1. Has management, with the oversight of those charged with governance, created and maintained a culture of honesty and ethical behaviour? Have they communicated and enforced integrity and ethical values? |  |  |
| 1. Are the responsibilities and authority from the senior management to staff level clearly defined? |  |  |
| 1. Has management considered the competence levels for particular jobs and how those levels translate into requisite skills and knowledge? |  |  |
| 1. Has management participated in the design and implementation of controls for appropriate management structure? |  |  |
| **B. Codes of conduct** |  |  |
| 1. Does management promulgate a written code of conduct, applicable to both management and staff, to serve as a benchmark for management’s and staff’s attitudes and behaviour? |  |  |
| 1. Is the code communicated throughout the organisation? Is it periodically acknowledged by the employees? Have the employees subscribed to the relevant Code of Conduct? |  |  |
| 1. Are employees informed of what they should do if they encounter improper behaviour? |  |  |
| 1. Are there written policies to regulate management’s dealings with employees, suppliers, and other stakeholders? |  |  |
| 1. Is there a written policy in respect of declaring related-party transactions? |  |  |
| **C. Management’s attitude to internal controls** |  |  |
| 1. Does management encourage and act on independent assessments of the control environment and internal controls? For example, are audit reports and government instructions reviewed and responded to at management committee level? Are internal audit reports on internal controls encouraged by senior management and responded to at management committee level? |  |  |
| 1. Is there an appropriately constituted audit committee with oversight of internal and external audit arrangements, and a remit to consider the operation of internal controls? |  |  |
| 1. Does management respond robustly to breaches of codes of conduct and law? And is there communication throughout the organisation of disciplinary action taken as a result of breaches? |  |  |
| 1. Does management ever override normal procedures, codes, internal controls, etc.—for instance, to make procurements without following procurement procedures or appoint personnel without a media announcement? Are such overrides documented and investigated? |  |  |
| 1. Does management provide adequate resources for internal audit work? (Consider whether the internal audit function is of appropriate size, quality and independence.) |  |  |
| **D. Recruitment, retention and remuneration of senior staff** |  |  |
| 1. Are vacant senior positions widely advertised within the pool of suitably qualified individuals (internally and/or externally)? |  |  |
| 1. Are promotion and appointment mechanisms transparent and based on objective and appropriate criteria so as to prevent undue patronage and nepotism? |  |  |
| 1. Is there independent review of remuneration? |  |  |
| 1. Are factors other than achievement of short-term performance targets included in performance appraisals? |  |  |
| 1. Are integrity and ethical criteria included in performance appraisals? |  |  |
| 1. Is there an independent review of the function of key officers (i.e. by internal audit or any external party)? |  |  |
| 1. Are there job descriptions? If so, do they contain sufficient reference to control-related responsibilities? |  |  |
| 1. Are executive functions reserved to appropriate level of management? |  |  |
| 1. Do organisations have appropriate motivation and retention policies for employees? |  |  |
| 1. Are recruitment policies set out in writing? |  |  |
| 1. Are there appropriate procedures to verify candidate’s experience, qualifications and references? Are there appropriate committees constituted for recruitment? |  |  |
| 1. Are new employees made aware of their responsibilities and management’s expectations of them, preferably through a detailed written job description? |  |  |
| 1. Do performance reviews cover the achievement of developmental and training needs, and future developmental and training requirements of employees? |  |  |
| 1. Are there appropriate disciplinary procedures for transgressions of the organisation’s code or other unacceptable employee behaviour? |  |  |
| **E. Management oversight of operations** |  |  |
| 1. Is there a clearly defined management/organisation structure with clear reporting lines encompassing all of the organisation’s function and staff? |  |  |
| 1. Are there up-to-date procedure manuals covering both the operational and financial accounting procedures? |  |  |
| 1. Does management establish financial and physical targets for the organisation? |  |  |
| 1. Is there a practice of preparing management accounts/performance appraisal reports? If there is, do they have an appropriate level of commentary/budget comparison prepared on a regular and timely basis? |  |  |
| 1. Are the management accounts drawn up from the same accounting records that form the basis of the audited financial statements? |  |  |
| 1. Do the accounting records appear to be well ordered and complete, and are financial reconciliations carried out on a regular basis? |  |  |
| 1. Is the budget setting process:   – Set out in a procedural manual?  – Carried out by suitable personnel?  – Accepted by line managers and those personnel who have operational responsibility? Subject to senior management approval? Conducive to budget discipline? |  |  |
| 1. Are there relevant and reliable performance measures/indicators in place? |  |  |
| 1. Does senior management give appropriate consideration to the process and results of external audit and the financial statements? |  |  |
| 1. **ENTITY’S RISK ASSESSMENT PROCESS** | | |
| 1. Are there documented manuals or established ad hoc processes in identifying, assessing and responding to business risks? |  |  |
| 1. Does the process involve individuals with appropriate authority and holistic knowledge about the entities strategic and operational activities? |  |  |
| 1. Does the audited entity have a process in identifying operational risks relevant to financial reporting objectives? |  |  |
| 1. Does the audited entity assess the significance and likelihood of occurrence of the identified business risks? |  |  |
| 1. Are the assessed business risks properly addressed? |  |  |
| 1. Is the entity’s risk assessment process appropriate in the circumstances given the nature and complexity of the entity?\* |  |  |
| **\*Note:** If the audit team identifies risks of material misstatements that the audited entity’s risk assessment process would normally identify but failed to identify, the audit team should investigate the cause and consider the implication in letter (f) above. | | |
| 1. **THE ENTITY’S PROCESS TO MONITOR THE SYSTEM OF INTERNAL CONTROL** | | |
| 1. Does the audited entity have a designed process for periodic or ongoing monitoring activities? |  |  |
| 1. Do the monitoring activities provide timely information about the effectiveness and deficiencies in internal controls? |  |  |
| 1. Are the identified deficiencies provided with remedial actions and timely communicated to those responsible individual(s)/unit(s)? |  |  |
| 1. Does the audited entity have an appropriate and functioning internal audit function?\* |  |  |
| 1. Does the audited entity has mechanism to ensure reliability and relevance of the sources of information used for monitoring activities? |  |  |
| 1. Is the audited entity’s process to monitor the system of internal control appropriate in the circumstances, including the frequency of monitoring, given the nature and complexity of the entity? |  |  |
| **\*Note**: In assessing internal audit function in letter (d), the audit team refers to Section 3.4 of AWP 5.1 and AWP 5.1a. | | |
| 1. **THE INFORMATION SYSYEM AND COMMUNICATION** | | |
| 1. Does the audited entity have defined information system and processing activities (significant classes of transactions), either manual or automated, that are relevant to financial reporting (e.g., through process manuals, policies & procedures) and supporting the preparation of the financial statements?\* |  |  |
| 1. Are these information system and processing activities assigned to appropriate and competent individuals?\* |  |  |
| 1. Do the policies define nature of data or information to be processed and the specific processes to maintain their integrity?\* |  |  |
| 1. Does the audited entity have appropriate and working communication protocols that support the preparation of financial statements and related reporting responsibilities in the information system and other components of the system of internal control among people within the entity, management and those charged with governance, and external parties as appropriate? |  |  |
| **\*Note:** The assessment of these questions is based on the understanding of the processes that should be documented using AWP 5.3. | | |
| 1. **CONTROL ACTIVITIES** | | |
| 1. Does the audited entity establish controls that can address the significant risks of material misstatements?\* |  |  |
| 1. Does the audited entity establish controls over journal entries, including non-standard journal entries used to record non-recurring, unusual transactions or adjustments?\* |  |  |
| 1. Are there other controls established that are relevant in addressing the risk of material misstatements?\* |  |  |
| 1. Are the designed manual and/or automated control activities (e.g., authorisations and approvals, reconciliations, verifications, segregation of duties, physical or logical controls) appropriate in preventing, detecting and correcting material misstatements?\* |  |  |
| 1. Are the relevant manual and/or automated control activities existing and actually implemented?\* |  |  |
| **\*Note:** Assessment of these questions is based on the understanding of the processes that should be documented using AWP 5.3. Identified control activities that are relevant in the audit are documented in AWP 5.5. | | |

**Guidance for completing documentation of the evaluation of the entity’s system of internal control**

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| Overall objective of completing the template | The overall objective of this audit working paper is to evaluate the components of the entity’s system of internal control, which will have an impact on assessing the risk of material misstatement in the financial statements. |
| Applicable ISSAI | ISSAI 2315 |
| Guidance | This template will assist the audit team in having a general understanding of the entity’s system of internal control. The audit team may customise the template to integrate the peculiarities in the public sector within its jurisdiction, especially when there are specific requirements in the establishment of internal control system for the government. |
|  | |  |  | | --- | --- | | Column 1 | This column provides a suggested checklist for evaluating each component of the system of internal control, which can be modified by the audit team as necessary. | | Column 2 | Using the suggested checklist, the auditor can record the answer to Column 1 as Yes, No, or Not Applicable. It is suggested that this evaluation be done based on review of the documents, observations and interviews with management and other relevant staff in the entity. If the answer is Yes, it needs to be supported by relevant evidence gathered from the entity, which may also include records of interviews. Not Applicable is suggested as a possible answer in case the auditor plans to use this as a standard checklist, in which case some items therein would not be applicable to the particular audit. | | Column 3 | If the answer to specific checklist(s) under column 1 is recorded as No under Column 2, the auditor needs to record how that will affect the assessment of the risk of material misstatement in Column 3. This should then be traced to the working paper on ROMM (referred to here as AWP 5.4). Take note that if there are deficiencies in internal control which are considered significant, the audit team is required to fulfil their communication responsibilities in accordance with ISSAI 2265. | |
| Recording the evidence of evaluator and reviewer | The Table indicating the names of the person who evaluated the components of the system of internal control and the reviewer needs to be completed at the end. One of the team members could evaluate the internal controls, in which case she/he should sign off as evaluator.  The reviewer, usually the audit engagement supervisor, should sign off this document to ensure that the work done by the team has been reviewed accordingly. |