

Preparing for an Audit

INTERNAL CONTROLS

Auditors must gather information about your organization's internal controls and will use a variety of procedures to gather the information that they need. These questions are designed to help you put your thoughts together and answer questions that are commonly asked. Taking the time to think about these questions prior to the audit will not only give you a better understanding of the strengths and weaknesses of your internal controls, but also contribute to a more efficient, less costly audit.

Significant Classes of Transactions

Make a list of your organization's significant classes of transactions (i.e. sales, cash receipts, disbursements, payroll).

For each transaction type, prepare answers to the questions below.

- How are significant classes of transactions authorized, captured, and processed?
- What areas of processing are most susceptible to errors?
 - Review errors that have occurred in the past. What was the cause? Has the source of the problem been addressed?
 - Review internal control deficiencies identified in past audits. What type of errors may happen as a result of these control deficiencies?
- What are the key controls that you depend on to prevent or detect errors?
 - When errors are detected, what is the process for correction of accounting records?
- How are accounting records for these transactions reconciled to each other?
- Who is responsible for performing the key controls related to these transactions?
 - Do the responsible individuals have the ability to authorize or enter transactions into the accounting system?
 - If so, the organization bears a risk of fraud in this area. How does the organization mitigate this risk?



Risk Of Fraud

- What fraudulent actions are most common for organizations similar to yours?
- What fraudulent actions are most likely at your organization?
- What steps has the organization take to mitigate the risks of fraud?
 - When deciding how to reduce the risk of fraud, what thought process does leadership follow?

Financial Reporting Process

- What procedures do you perform that would allow you to identify material misstatements to the financial statements? How would you identify material misstatements affecting:
 - Significant assets and liabilities
 - Total assets and liabilities
 - Revenue
 - Net income
 - Important financial ratios such as working capital or inventory turnover
- What procedures are in place to allow you to identify all matters that should be disclosed in the notes to the financial statement? What controls are in place to make sure these items are properly described in the notes?
- How do you identify transactions or events that are outside the normal business transactions and require special accounting consideration? What steps do you take to ensure that these transactions are properly accounted for?
- How do you control the posting of journal entries and other adjustments to the general ledger to make sure they are authorized and proper?
- How do you identify changes to accounting rules that impact your organization? If you identify changes, what do you do to ensure that the new rules are applied correctly?

Culture and People

- How high of a priority do you place on each of the following items and why?
 - Preventing fraud
 - Creating and maintain a system that provides timely and reliable information needed to manage the organization
 - Providing timely, reliable, and transparent financial information to creditors, regulators and other third parties
- Do others in the organization understand the importance of the above items to management of the organization? How is this sense of importance communicated?
- How do you promote honesty and ethical behavior within the organization? What actions



do you take to ensure that others in the organization “get the message?”

- What steps do you take to attract and retain highly qualified individuals in key positions?
 - How do you know what the job requirements are for each key position?
 - How do you make sure the people in those positions maintain/enhance the skills and have access to the necessary resources to perform assigned tasks?

Maintaining Internal Control Effectiveness

- What steps are taken when you become aware of accounting errors? How do you investigate the underlying cause of those errors?
 - When addressing underlying causes, how do you evaluate and make necessary changes to your control system to reduce the risk of those same errors occurring in the future?
- When you discover a weakness in your accounting system or internal controls, what steps to do take to address these weaknesses?
 - What criteria do you use to decide whether to correct or “live with” systems or controls that are less than ideal

