

CONDUCTING  
THE  
ASSURANCE  
ENGAGEMENT



# Navigating this Presentation

## CONTENT COMPASS:

01 Learning Objectives

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02 Overview of an Assurance Engagement

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03 Planning an Assurance Engagement

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04 Performing an Assurance Engagement

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05 Next Meeting: Communicating Assurance Engagement Outcomes and Performing Follow-Up Procedures

# Learning Objectives



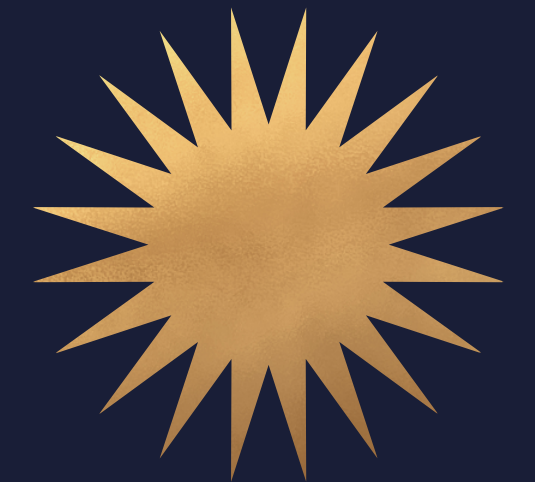
Describe key stages of assurance engagements and activities involved.



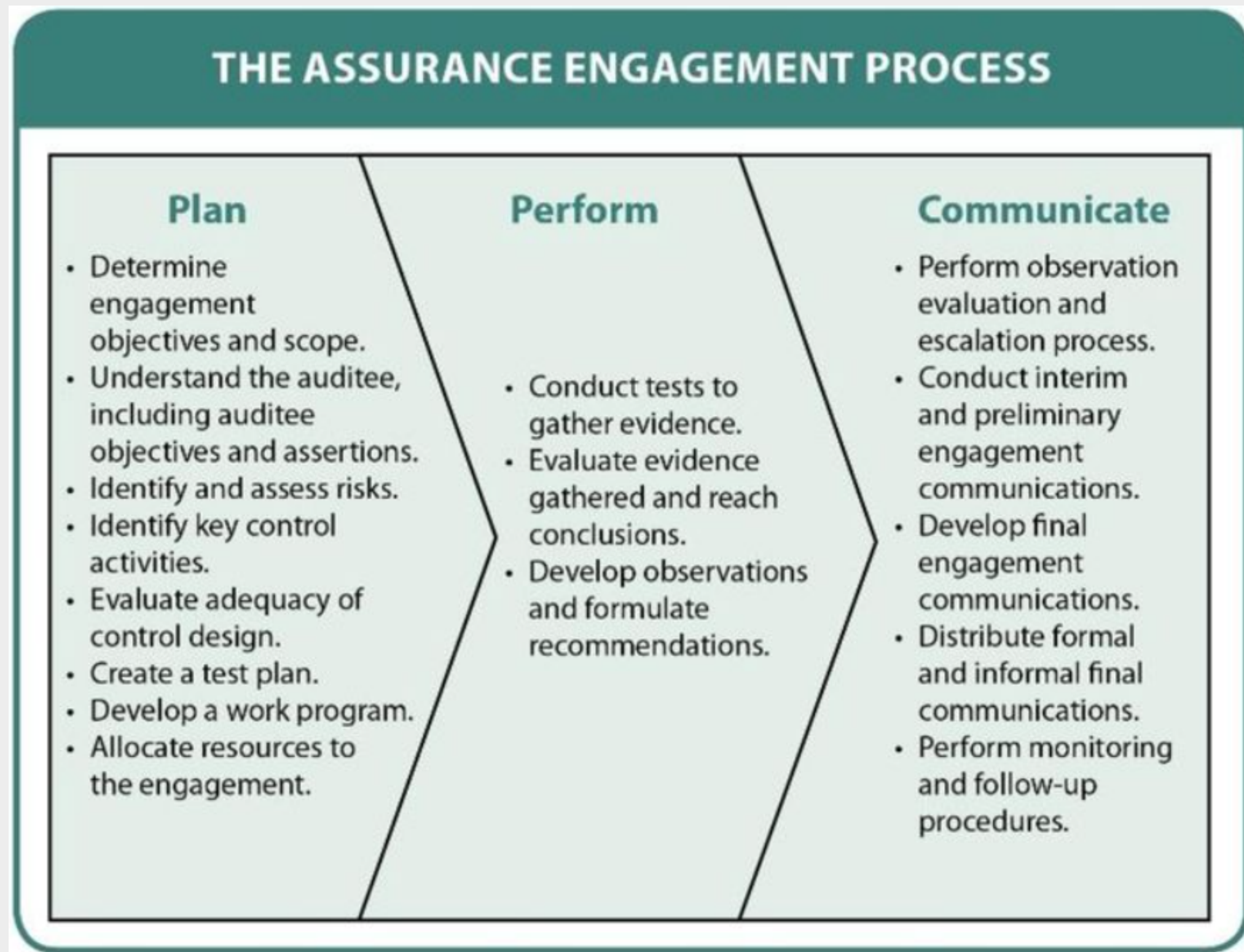
Determine engagement objectives and scope statements.



Describe how the purpose of an assurance engagement impacts the audit objectives.



# Assurance Engagements



# THE ASSURANCE ENGAGEMENT PROCESS

## Plan

- Determine engagement objectives and scope.
- Understand the auditee, including auditee objectives and assertions.
- Identify and assess risks.
- Identify key control activities.
- Evaluate adequacy of control design.
- Create a test plan.
- Develop a work program.
- Allocate resources to the engagement.

## Perform

- Conduct tests to gather evidence.
- Evaluate evidence gathered and reach conclusions.
- Develop observations and formulate recommendations.

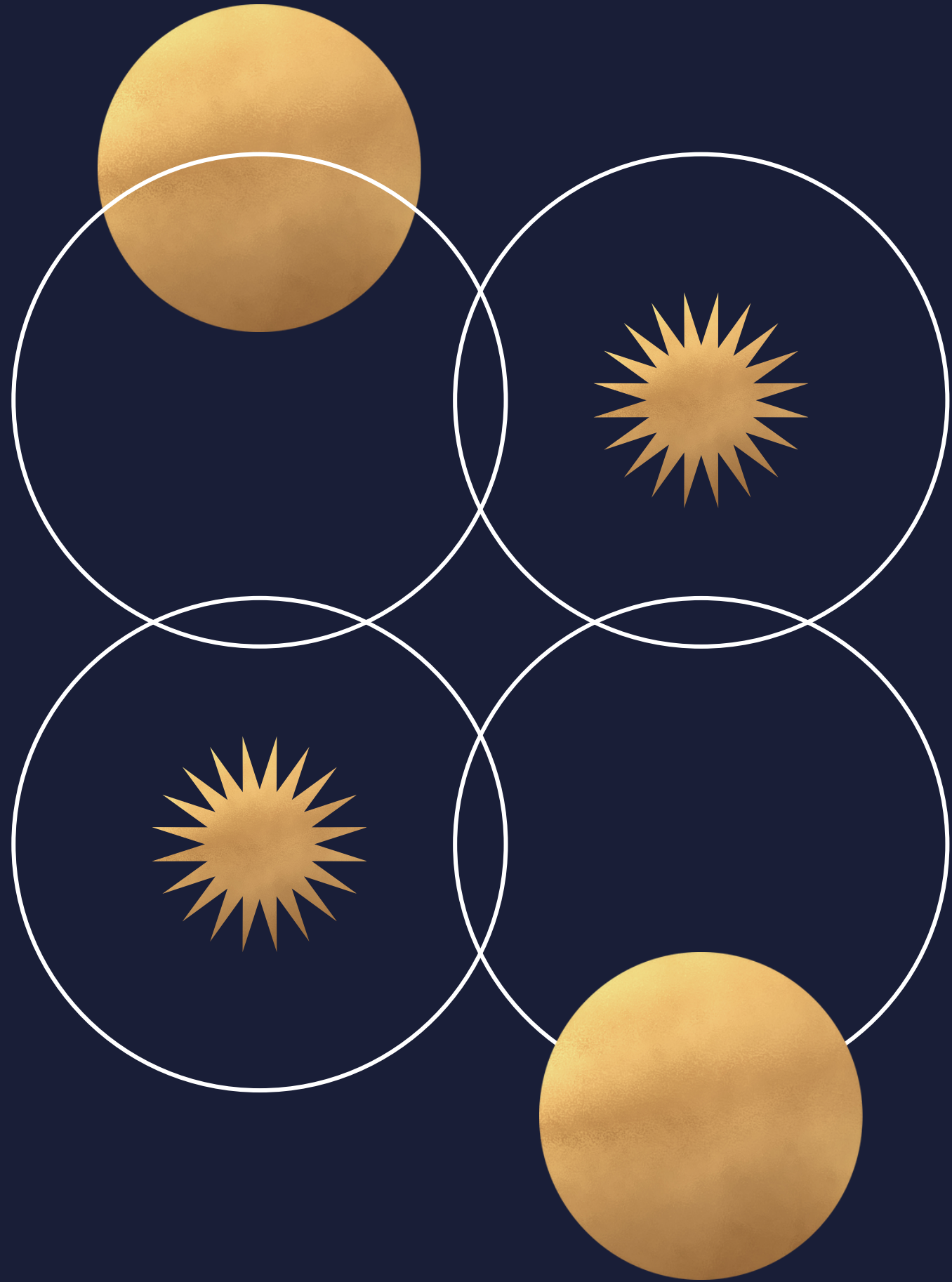
## Communicate

- Perform observation evaluation and escalation process.
- Conduct interim and preliminary engagement communications.
- Develop final engagement communications.
- Distribute formal and informal final communications.
- Perform monitoring and follow-up procedures.



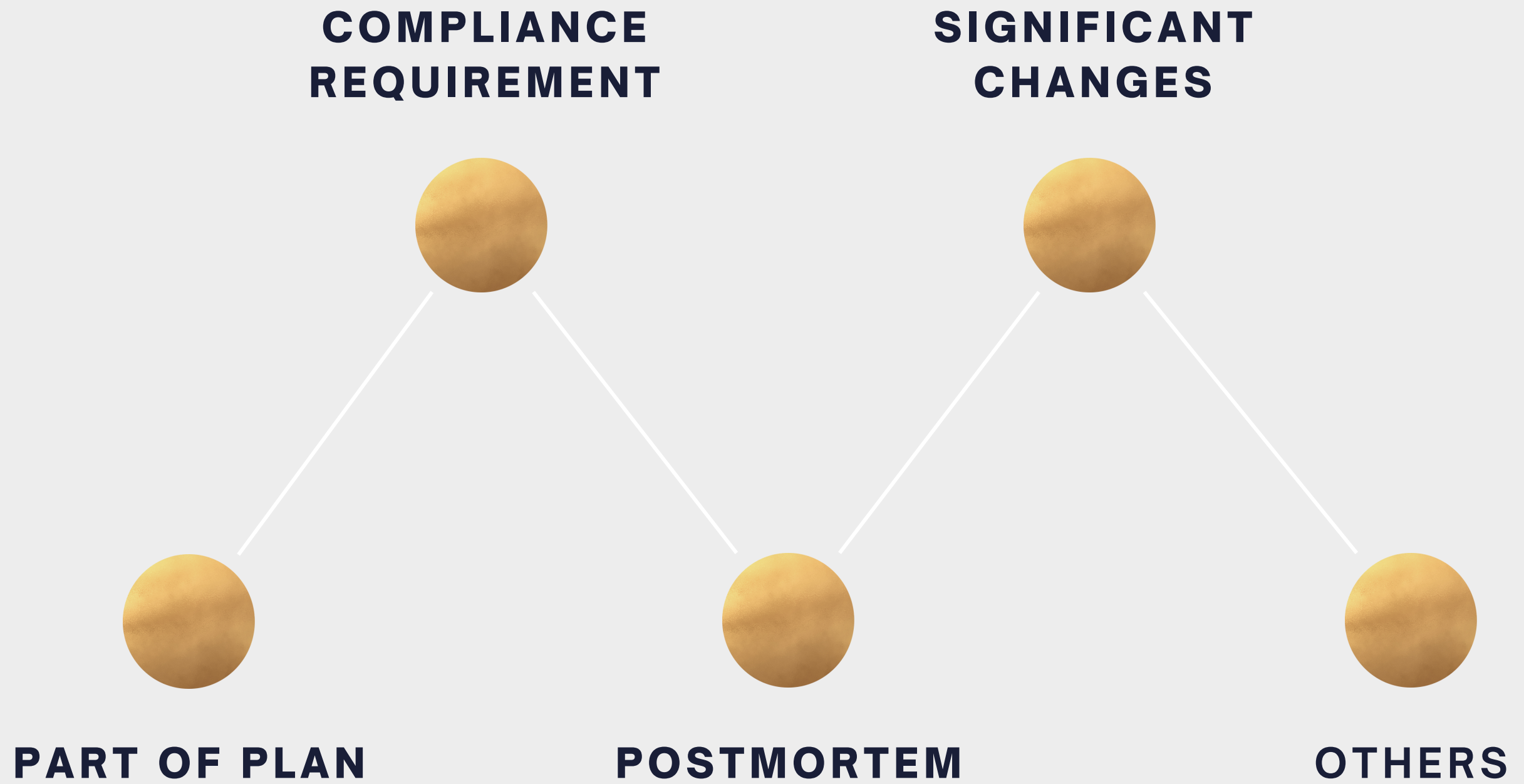
# Planning

1. Determine engagement objectives and scope
2. Understand the auditee
3. Identify and assess risks
4. Identify key controls
5. Evaluate adequacy of control design
6. Create a test plan
7. Develop a work program
8. Allocate resources



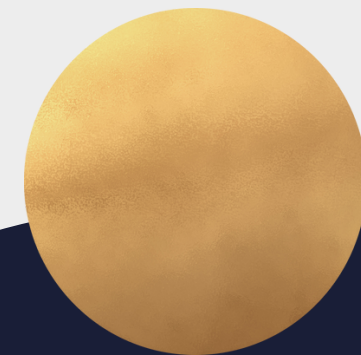
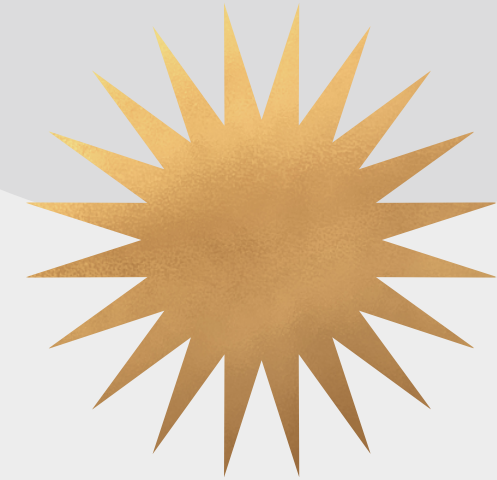
DETERMINE  
ENGAGEMENT  
OBJECTIVES  
AND SCOPE

# Reasons for Conducting an Engagement



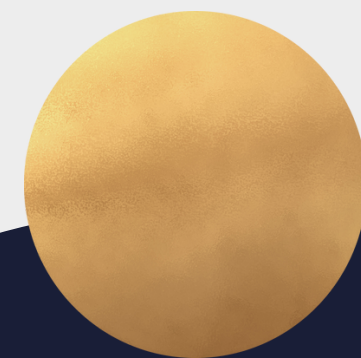
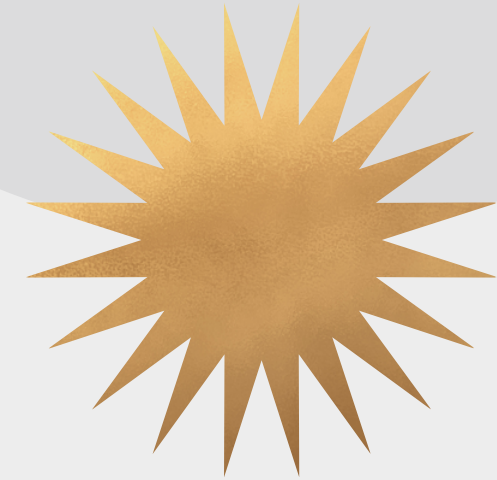
# Establishing Engagement Objectives

- Evaluate the design adequacy of...
- Determine the operating effectiveness of...
- Assess compliance with...
- Determine the effectiveness and efficiency of...
- Evaluate the accuracy of...
- Assess the achievement of...
- Determine the performance of...



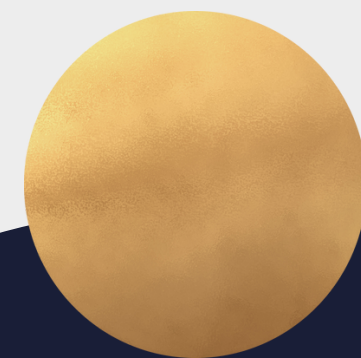
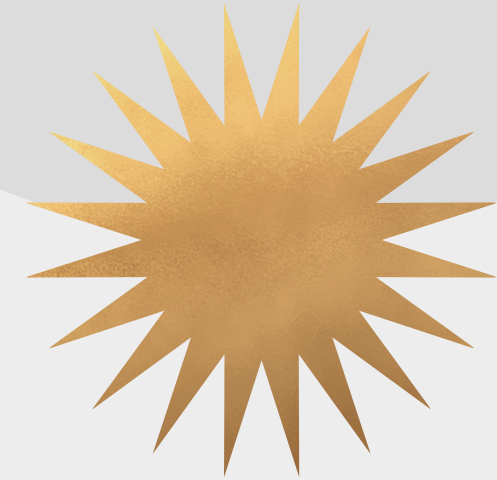
# Scope of the Engagement

- Boundaries of the process
- In-scope vs. out-of-scope locations
- Subprocess
- Components
- Time Frame



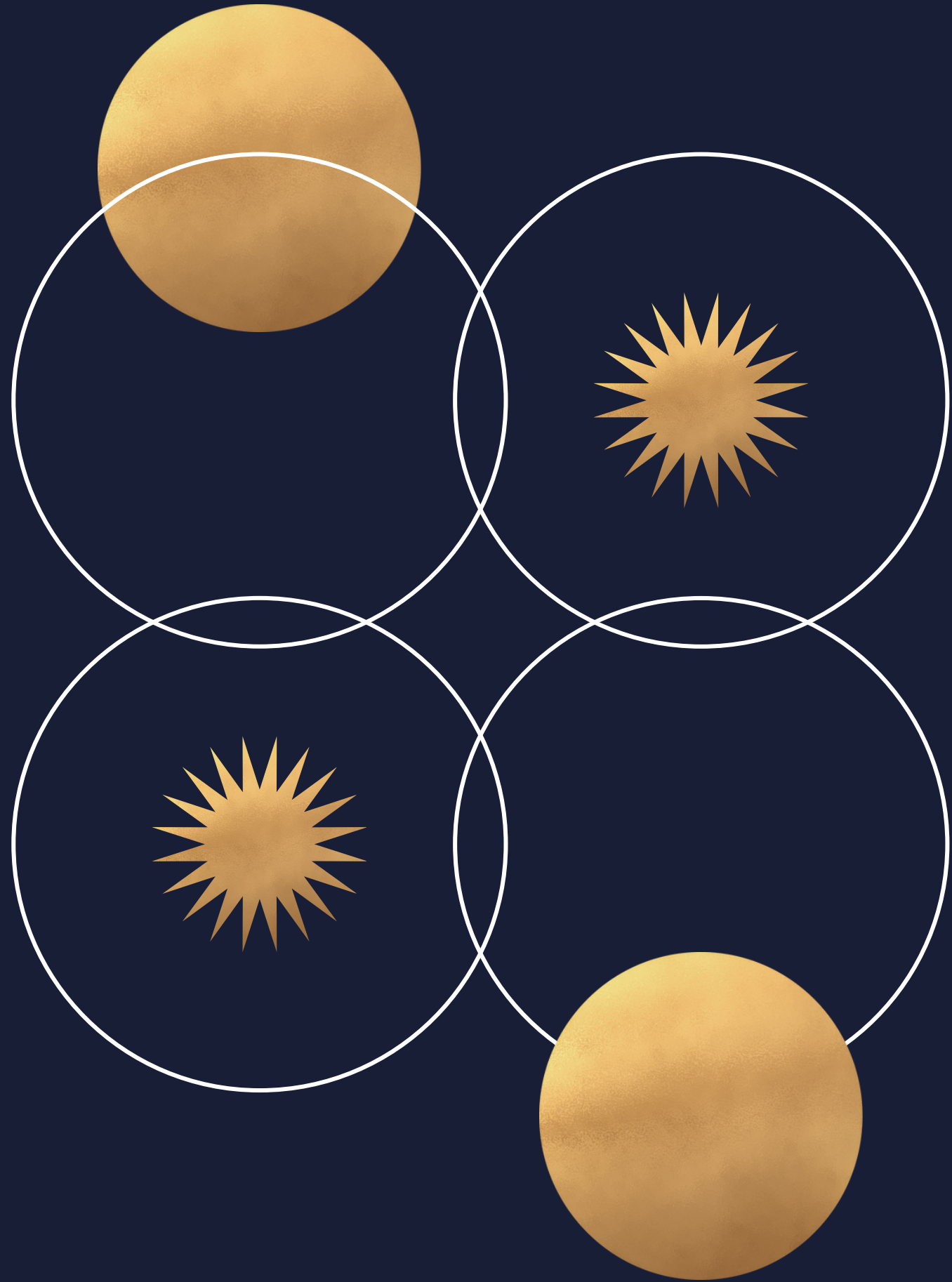
# Expected Outcomes and Deliverables

- Potential outcomes of the tests to be performed during the engagement.
  - Financial statement errors or
  - Control deficiencies
  - Shortfalls in objective achievement
  - Inefficiencies
  - Out-of-compliance situations



# Expected Outcomes and Deliverables

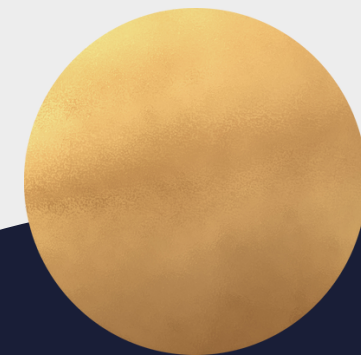
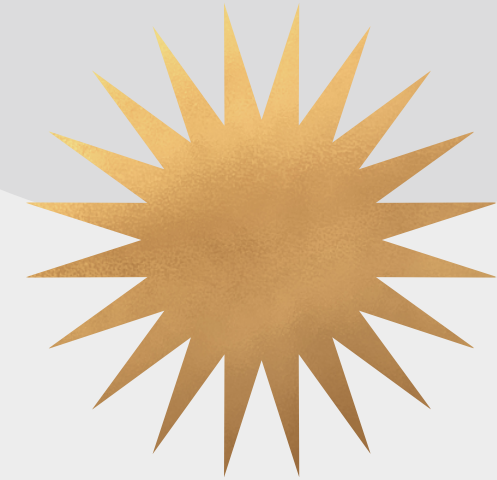
- Auditee expectations regarding engagement communications
  - Full-scope, internal reports
  - Internal memoranda
  - Reports for third-party use
  - Higher level of confidentiality



# UNDERSTAND THE AUDITEE

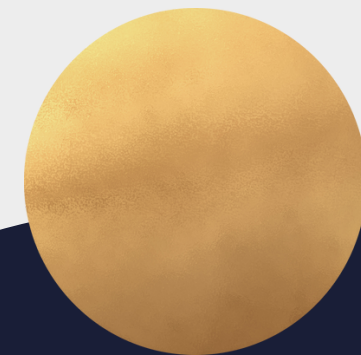
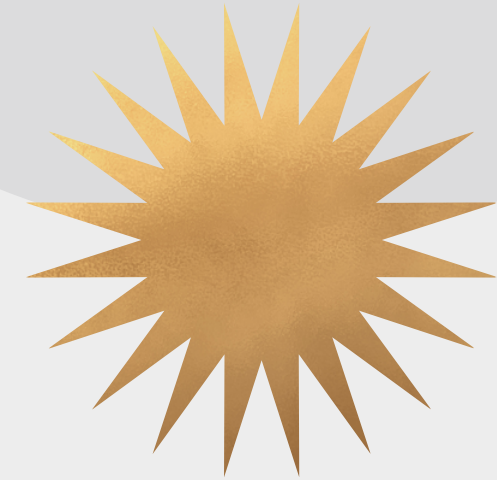
# Auditee Objectives

- Operations objectives
- Reporting objectives
- Compliance objectives
- Strategic Objectives
- Other objectives



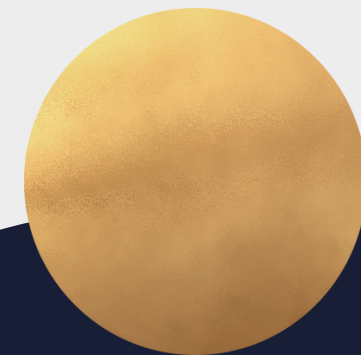
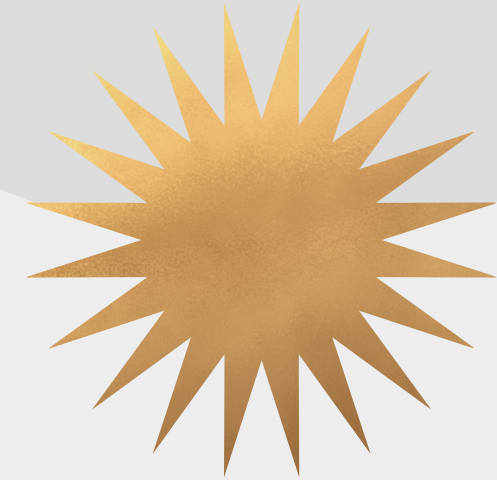
# Gathering Information

- Policies
- Manuals
- Org charts
- Job descriptions
- Process maps or flowcharts
- Narrative descriptions
- Copies of contracts
- Laws and regulations
- Others



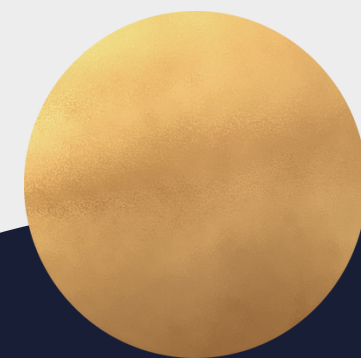
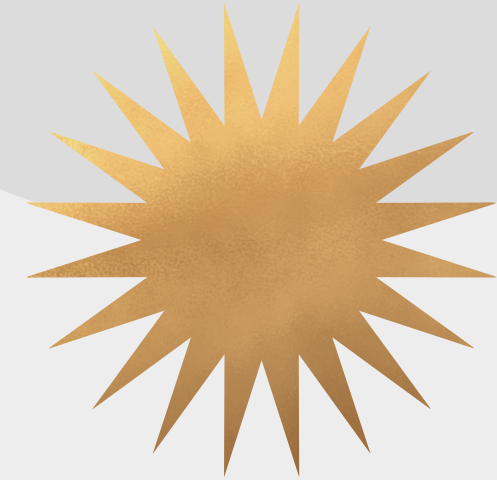
# Gathering Information

- What key tasks are you responsible for performing?
- What inputs (information, documentation, etc.) do you need to perform these tasks?
- What specifically, do you do with these inputs?
- What are the outputs that you produce from each task?
- Which other people or areas do you depend on as you perform these tasks?
- Which other people or areas depend on you performing these tasks effectively and timely?
- What information systems do you use when performing these tasks?
- How long does it take to complete each task?
- What types of exceptions or errors do you typically encounter?
- How do you handle these exceptions or errors?
- What other barriers or challenges do you typically encounter when performing these tasks?
- What do you do to remove the barriers or meet the challenges?
- In the end, how do you ensure that you perform the tasks correctly?



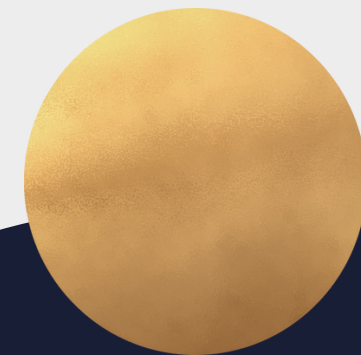
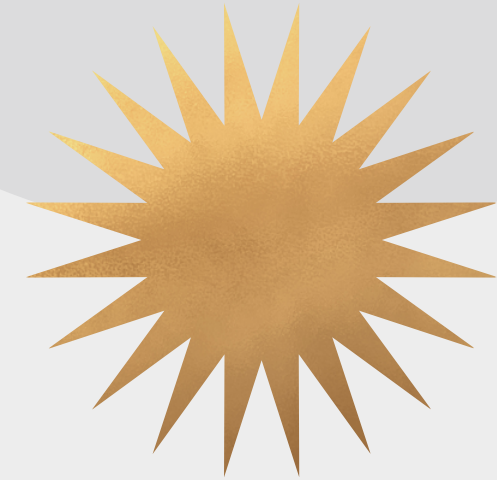
# Analytical Procedures

- Comparisons of financial information to prior periods
- Ratio analyses
- Comparisons of financial or nonfinancial information against budgeted information



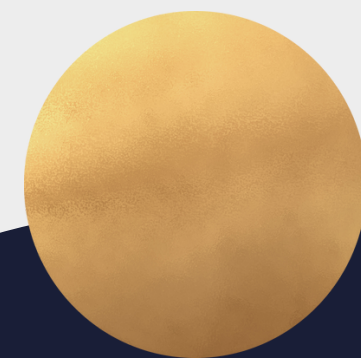
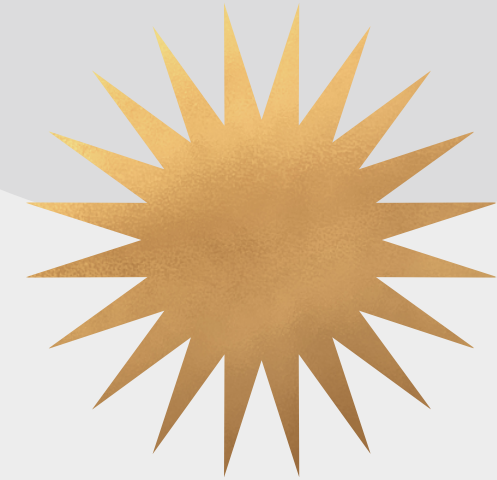
# Data Analysis

- Examples:
  - Number of late payments
  - Number of manual checks
  - Stratification of payment amount
  - Duplicate payment amounts to the same vendor



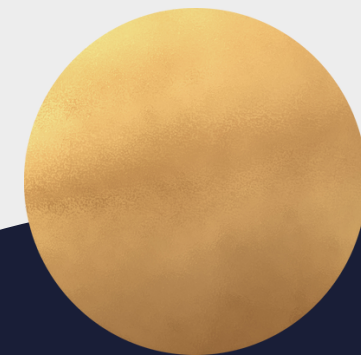
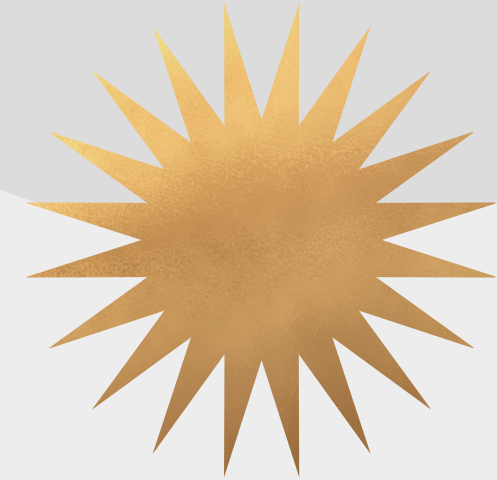
# Entity-level Control Analysis

Controls that operate across an entire entity and, as such, are not bound by, or associated with, individual processes.


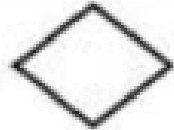



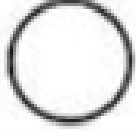
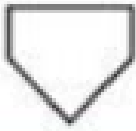




# Documenting Process Flow

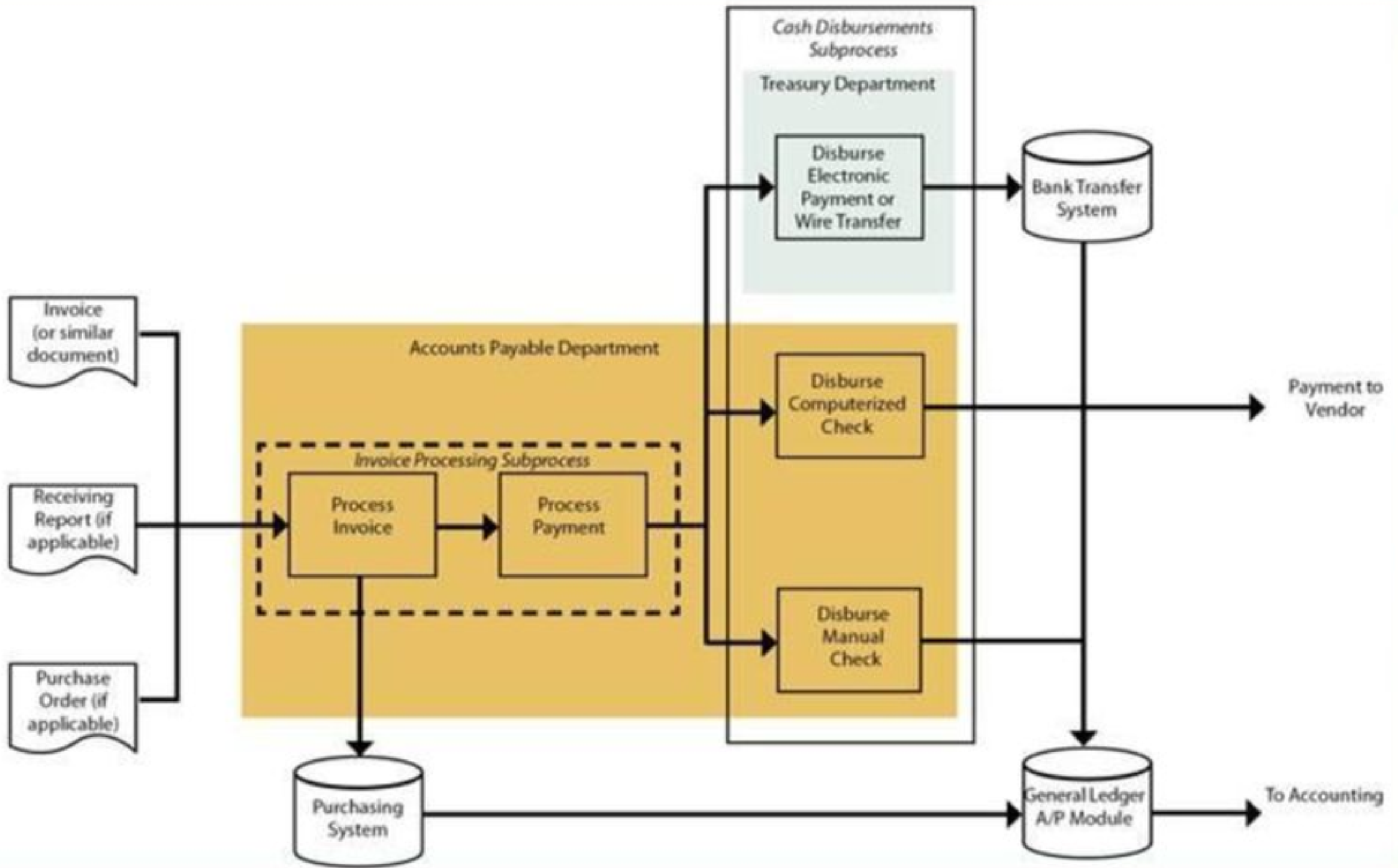
- Process maps
- Flowcharts
  - High-level
  - Detailed
- Narrative memoranda

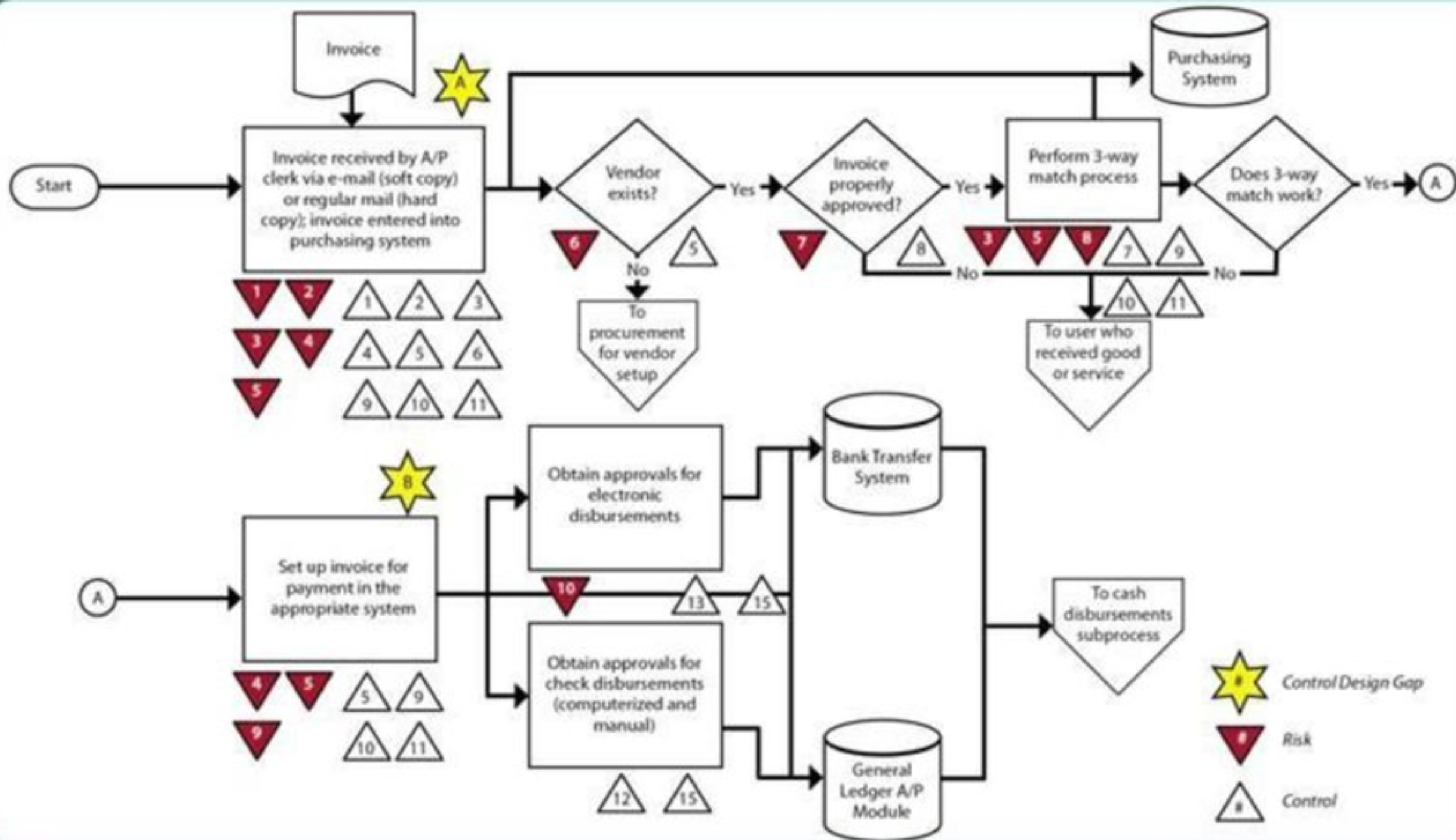


## COMMON FLOWCHARTING SYMBOLS

	<b>Process or operation</b> – A process, subprocess, or activity.
	<b>Decision</b> – Indicates alternative choices (for example, yes/no or accept/reject), each of which results in different flows of activities and/or documents.
	<b>Document</b> – A hard copy input source document or output report.
	<b>Flow line</b> – The direction of activities, workflow, information flow, documents, and handoffs.
	<b>Computer system or application</b> – Information technology that is used to store data, run an application, or perform other computer-based functions.
	<b>On-page connector</b> – Used to connect different parts of a flowchart on the same page without the use of flow lines.
	<b>Off-page connector</b> – Used to connect parts of a flowchart documented on different pages.
	<b>Terminator</b> – The start or end of a flow.
	<b>Annotation</b> – An explanatory note attached to a specific point in a flowchart.

HIGH-LEVEL FLOWCHART  
CASH DISBURSEMENTS PROCESS





**DETAILED FLOWCHART  
INVOICE PROCESSING SUBPROCESS**

## DETAILED FLOWCHART INVOICE PROCESSING RISKS

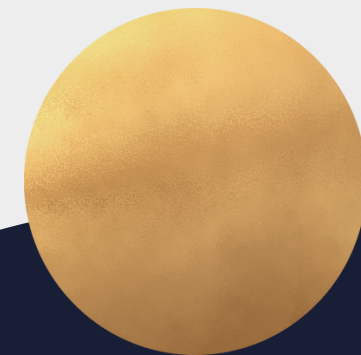
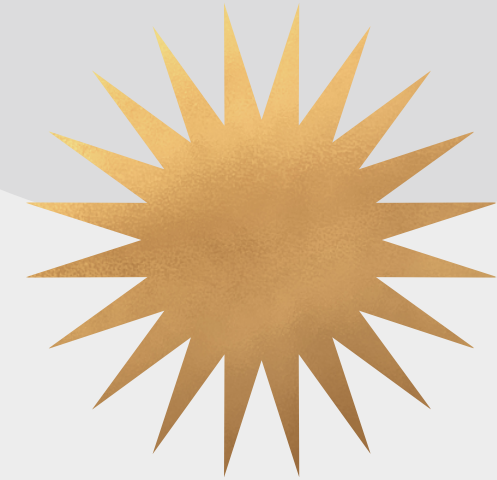
- 1 Invoice is not received timely by accounts payable, resulting in liability not being properly reflected in the financial statements.
- 2 Invoice is not processed timely by accounts payable, resulting in lost opportunities to take discounts or incurring late-payment fees.
- 3 Invoice information is entered inaccurately into the purchasing system, resulting in inaccurate or inappropriate payments.
- 4 Duplicate invoices are entered and processed for payment, resulting in payment for the same invoice twice.
- 5 Accounts payable personnel have inappropriate access to the various systems, allowing them to establish fictitious vendors, purchase orders, or establish fictitious vendors, create phony purchase orders, and make unauthorized payments.
- 6 Payments are processed to the wrong or a nonexistent vendor, resulting in late payments to the correct vendor, the need to collect refunds from the incorrect vendor, or a fraudulent payment.
- 7 Payments are processed for invoices that have not been approved yet, resulting in payment before the good or service is received.
- 8 Invoices are processed that do not match purchase orders, receiving reports, or other relevant documentation, resulting in establishing a liability and paying an incorrect amount.
- 9 Payments are made before the due date, resulting in lost time value of money.
- 10 Unauthorized payments are made, resulting in payments being made by a costly or inefficient means, or in a manner inconsistent to meet the cash flow requirements.

## DETAILED FLOWCHART — INVOICE PROCESSING CONTROLS AND DESIGN GAPS

-  As part of the month-end close process, the A/P manager will solicit information on unprocessed invoices and will prepare an accrual accordingly.
-  Once an approved invoice is entered, the system will automatically book the credit to A/P and debit to the appropriate expense or balance sheet account.
-  Open purchase orders are reviewed once per month by the purchasing manager to determine their status.
-  The A/P clerk runs a report at the end of each week showing invoices entered but not approved. For invoices outstanding more than a week, a reminder is sent to the user.
-  The purchasing system requires that all invoice fields are completed before processing is allowed. An invoice cannot be entered without a match to an approved vendor.
-  The purchasing system alerts the A/P clerk if the vendor number, invoice number, and invoice amount match an invoice previously entered.
-  The purchasing system confirms a match between quantities and prices on an invoice, purchase order, and receiving documents. If they do not match, the invoice is placed on hold.
-  Invoice approval limits are confirmed with department heads annually and updated if necessary.
-  A user name and password is required to access all of the systems. Passwords are subject to naming parameters, and must be changed every 90 days.
-  System access rights are reviewed semiannually with department heads to ensure access capabilities align with job responsibilities.
-  A/P personnel cannot access the vendor masterfile, nor can they make changes to previously entered purchase order and receiving information.
-  Only the A/P manager can initiate the processing of a computerized check batch.
-  Only treasury department personnel are entitled to process bank transfers.
-  The purchasing system interfaces with the general ledger A/P module and the bank transfer system.
-  Computerized checks over US \$50,000 require a manual signature of the treasurer. Computerized checks over US \$100,000 require a manual signature of the CFO. Manual checks require dual signatures from the treasurer and CFO. The treasurer must authorize individual bank transfers in excess of US \$100,000.
-  There is no check with users to determine whether any goods or services have been received but not invoiced yet (engagement observation written up on working paper Z-1).
-  While the purchasing system does alert the A/P clerk to potential duplicate invoices, it does not prevent the A/P clerk from continuing to process such an invoice (engagement observation written up on working paper Z-2).

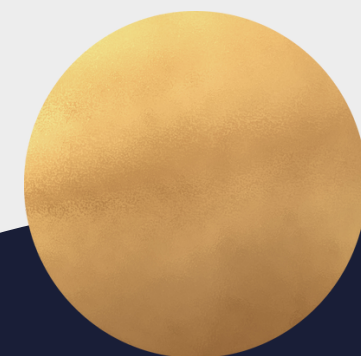
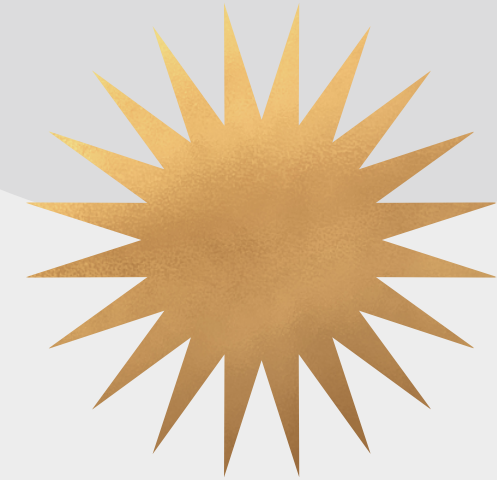
# Narrative Memoranda

- More appropriate when:
  - Simple process
  - Complicated steps
  - Process owner request
  - More efficient
- Should generally include:
  - Overall description of the process
  - Key inputs
  - Key steps in the process
  - Key outputs
  - Risks that threaten the process
  - Key controls



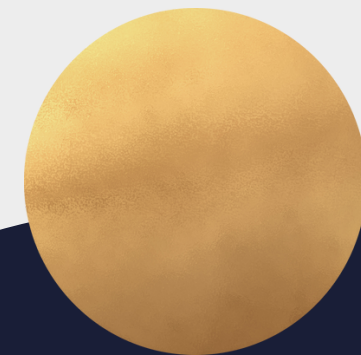
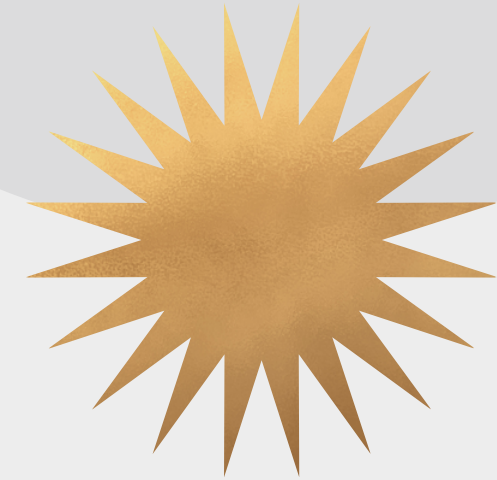
# Identifying Key Performance Indicators

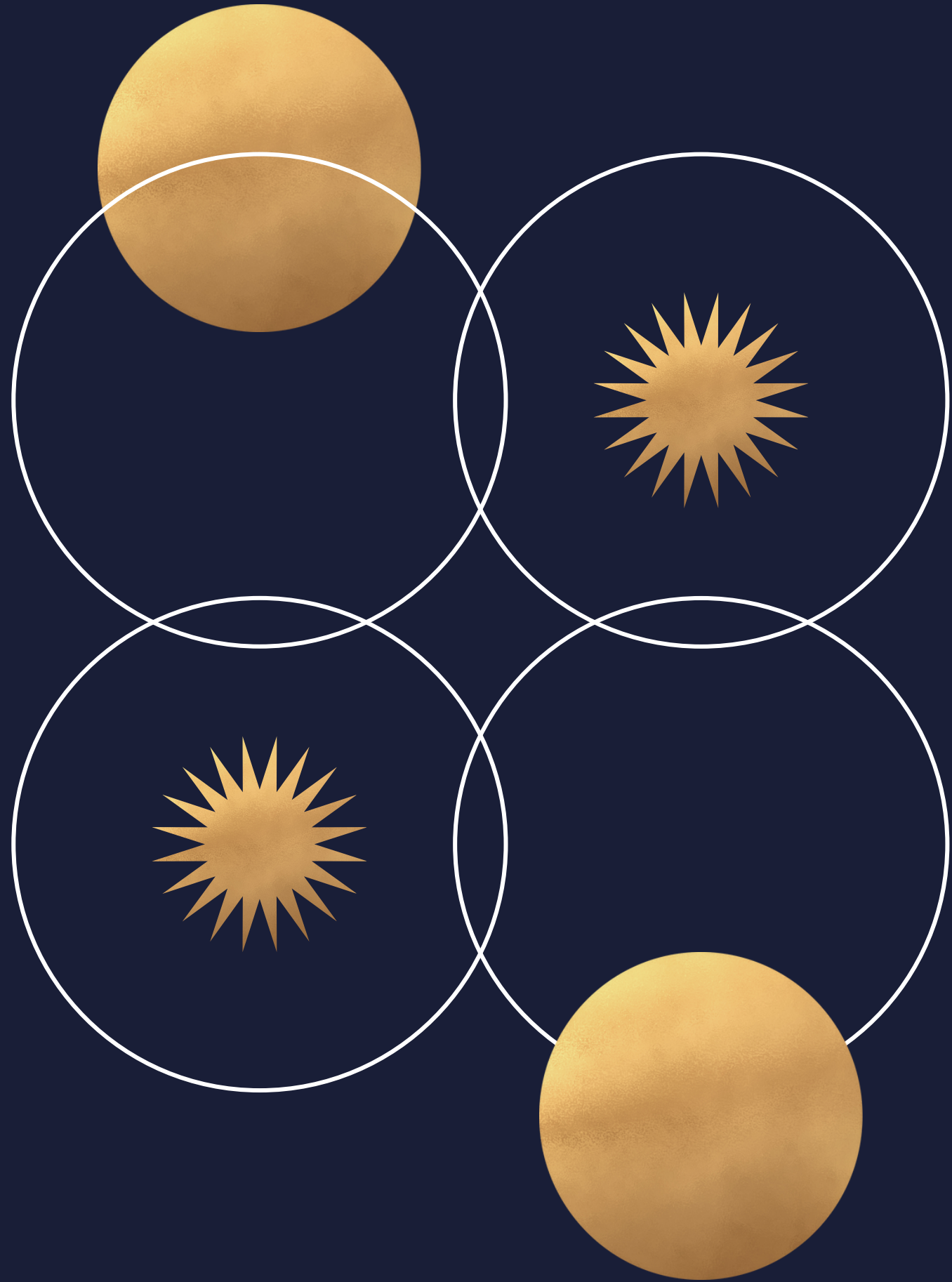
- Relevant
- Measurable
- Available
- Aligned
- Articulated



# Evaluating Process-level Risks

- Identify potential fraud scenarios
- Understand potential fraud impact
- Determine whether to test for specific fraud risks

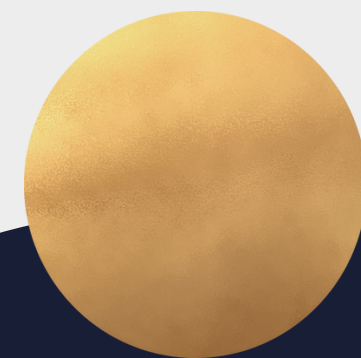
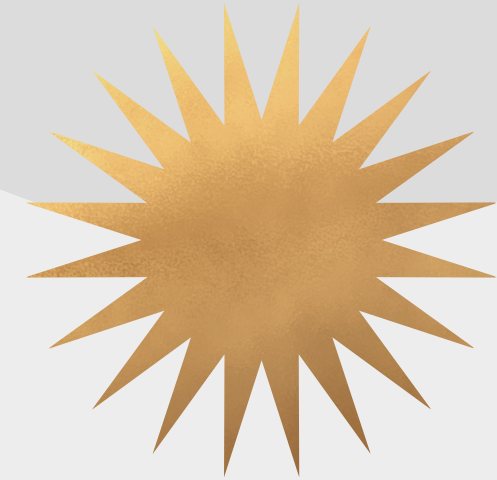


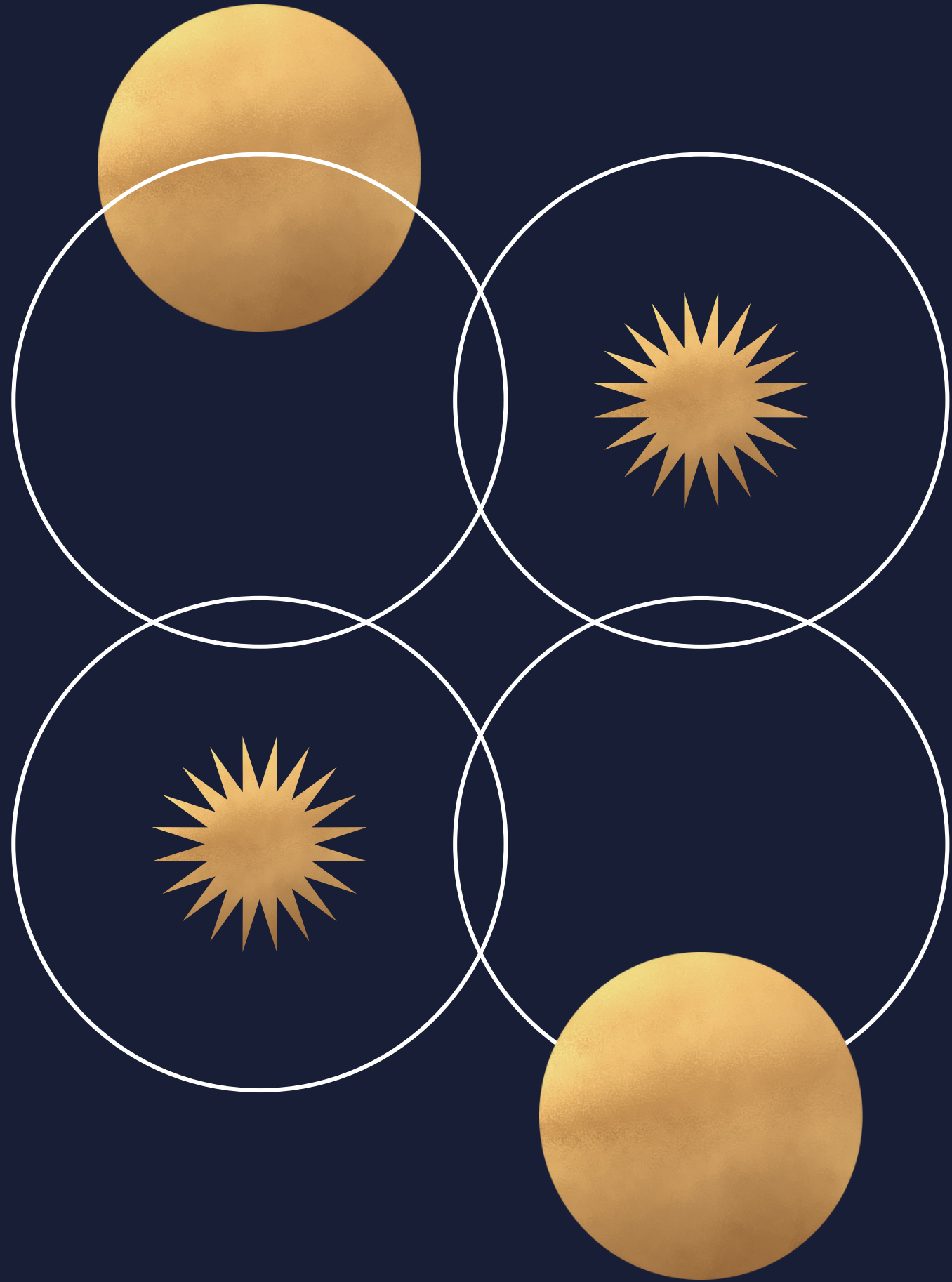


# IDENTIFY AND ASSESS RISKS

# Identify and Assess Risks

- Identifying Process-Level Risk Scenarios
- Defining Process-Level Risks
- Evaluating the Impact and Likelihood of Risks
- Understanding Management's Risk Tolerance

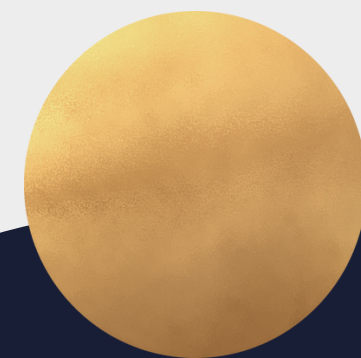
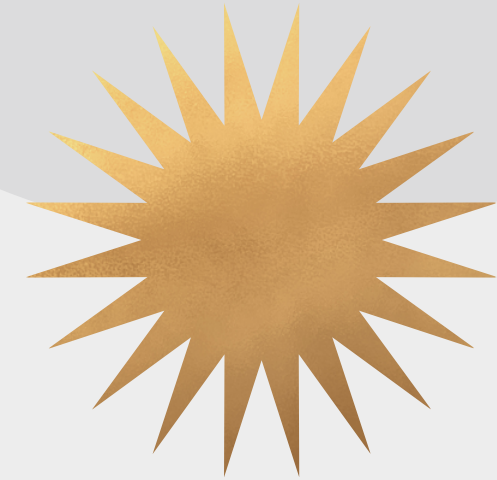




# IDENTIFY KEY CONTROLS

# Identify Key Controls

- Approving
- Calculating
- Documenting
- Examining
- Matching
- Monitoring
- Restricting
- Segregating
- Supervising

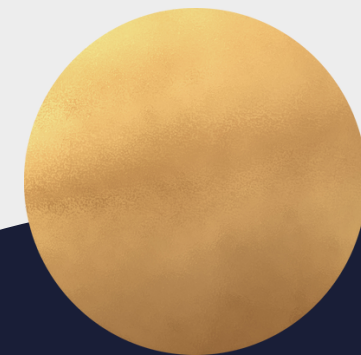
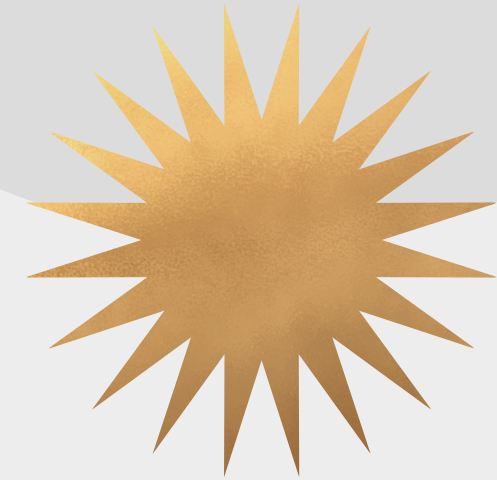


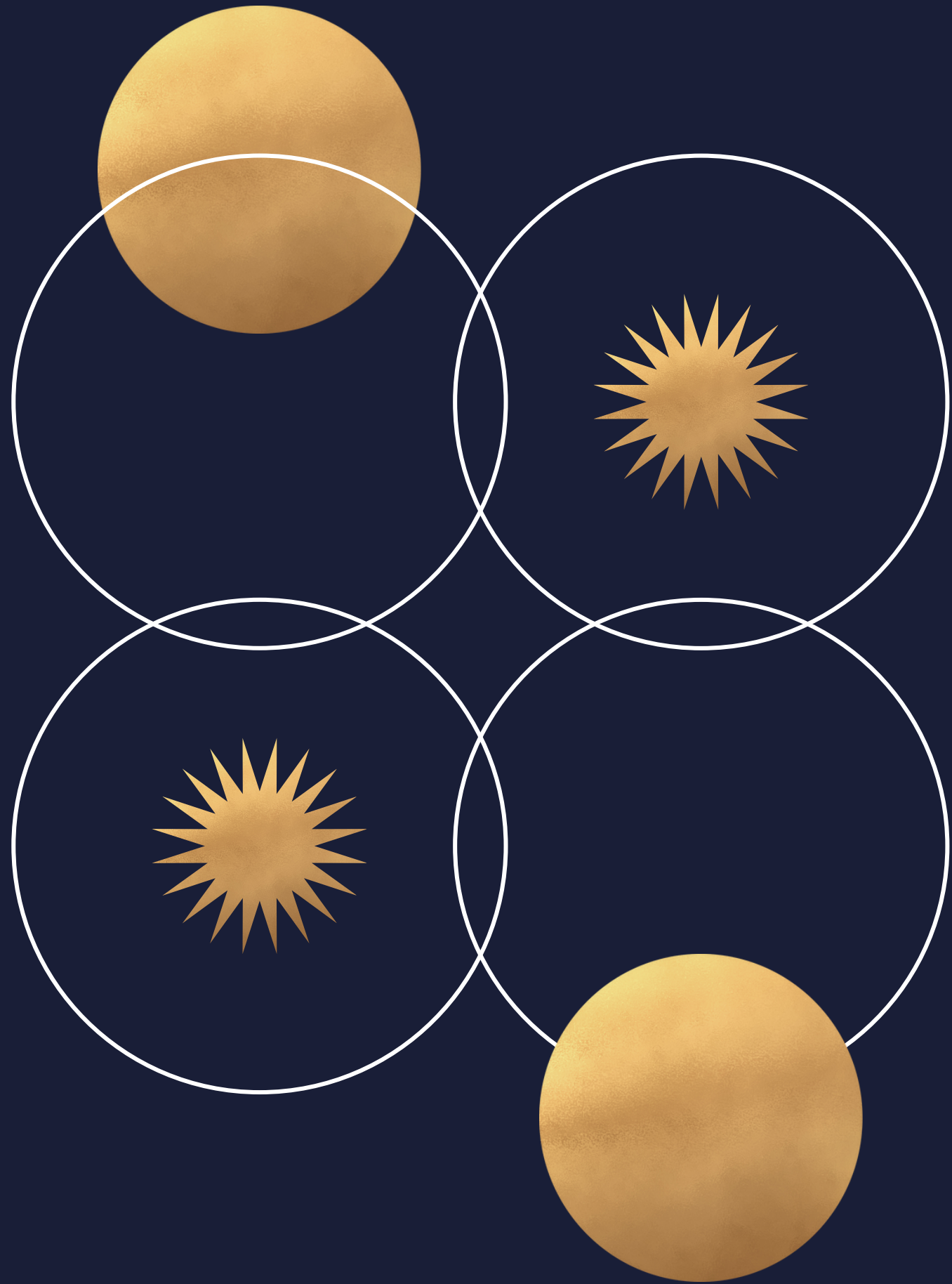
# Identify Key Controls

- No checklist or formula
- Judgmental process
- “If not performed as designed, which of these controls would likely result in the inability to achieve the process-level objectives?”

# Identify Key Controls

- The internal auditor must have a clear understanding of the process-level objectives.
- Other compensating controls should be considered.
- The effect of one control on other controls also must be considered.
- The impact of entity-level controls also should be considered.
- Redundant controls

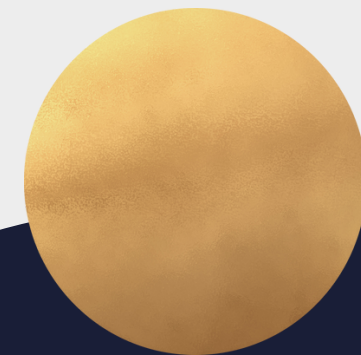
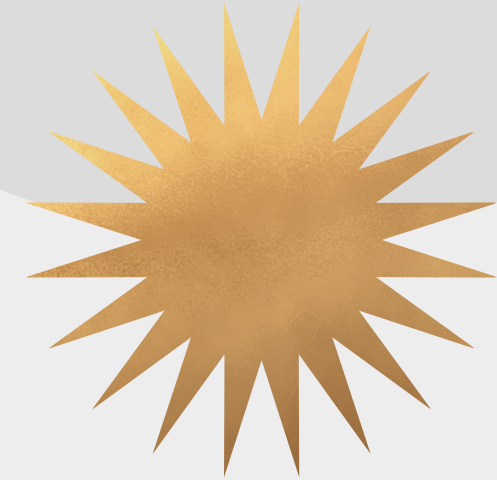




EVALUATE  
THE DESIGN  
ADEQUACY

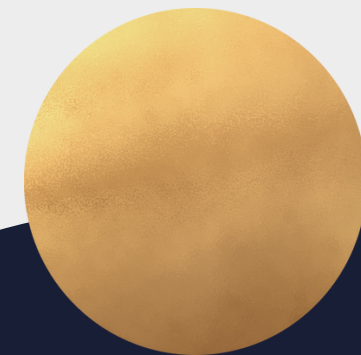
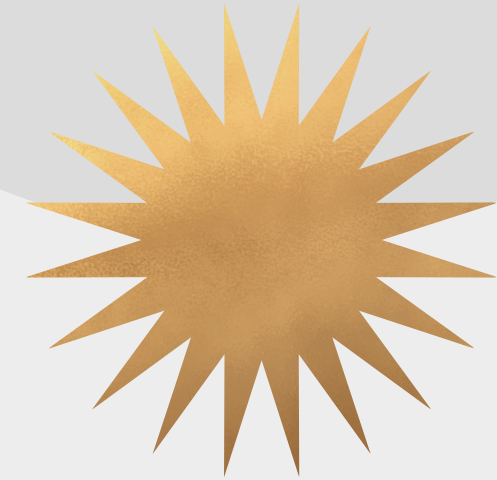
# Evaluate the Design Adequacy

- Does the internal auditor understand what an "acceptable level" of risk is, based on management's risk tolerance levels for the process?
- Do the key controls, taken individually or in the aggregate, reduce the corresponding process-level risks to acceptable levels?
- Are there additional compensating controls from other processes that further reduce risks to acceptably low levels?
- Does it appear that the key controls, if operating effectively, will support the achievement of process-level objectives?
- To the extent appropriate, does the process design address effectiveness and efficiency of operations, reliability of reporting, compliance with applicable laws and regulations, and achievement of strategic objectives?
- What gaps, if any, exist that impede the process?
  - What specific gaps exist in the design of the process?
  - What are the possible outcomes or effects of those gaps?



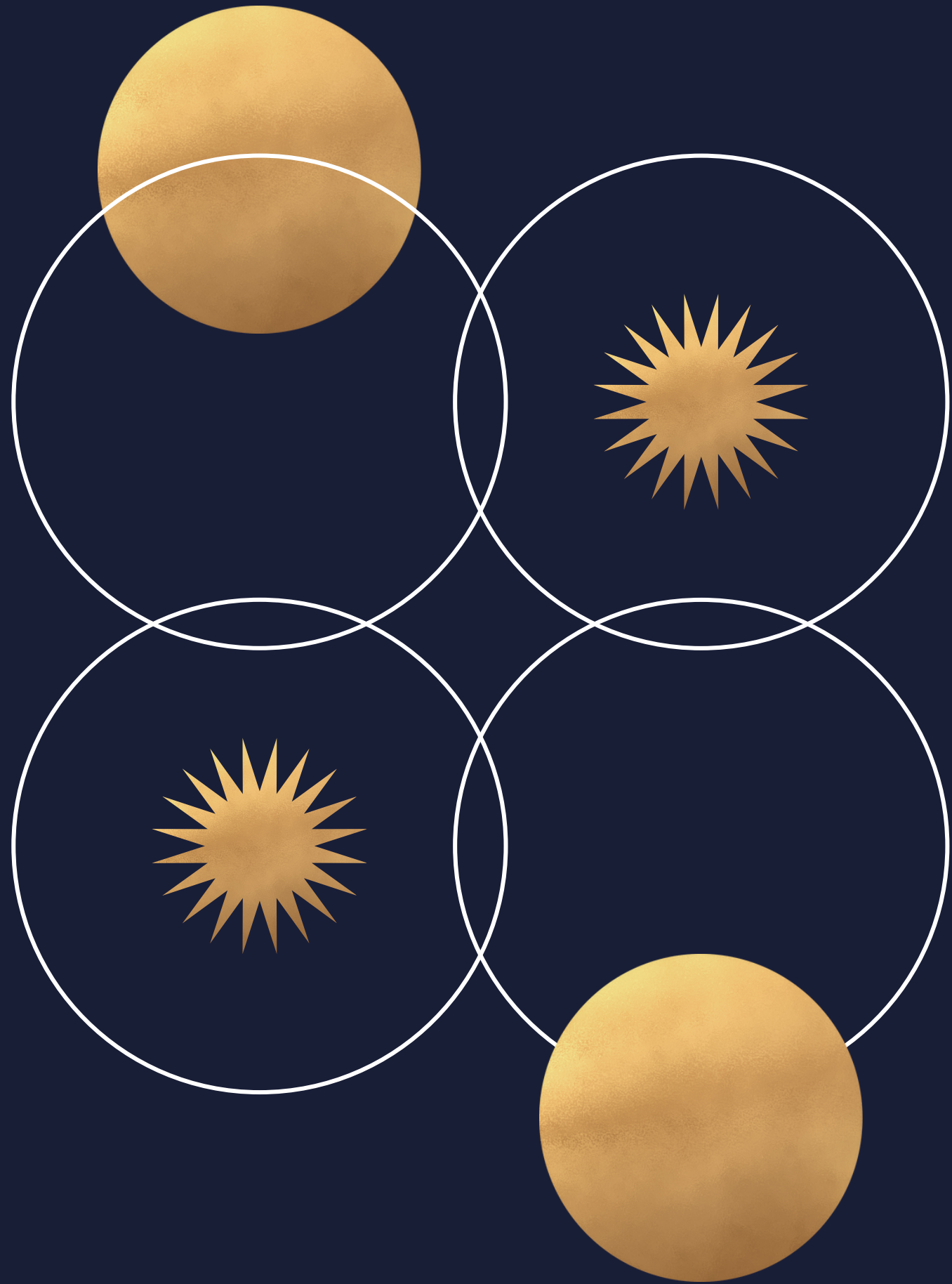
# Evaluate the Design Adequacy

- Auditor's judgment is typically one of the following:
  - The indicated key controls are designed adequately to manage this risk to an acceptable level.
  - The indicated key controls are not designed adequately to manage this risk to an acceptable level (describe design gap).
- Auditor's conclusion is typically one of the following:
  - Design is adequate; no significant gaps.
  - Design is adequate; however, gaps exist.
  - Design is inadequate; significant gaps exist



## EXAMPLE RISK AND CONTROL MATRIX

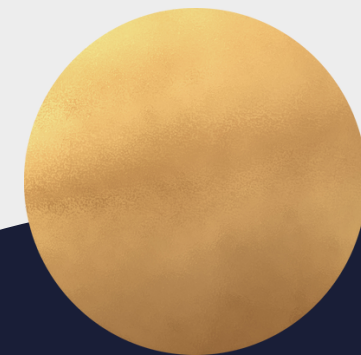
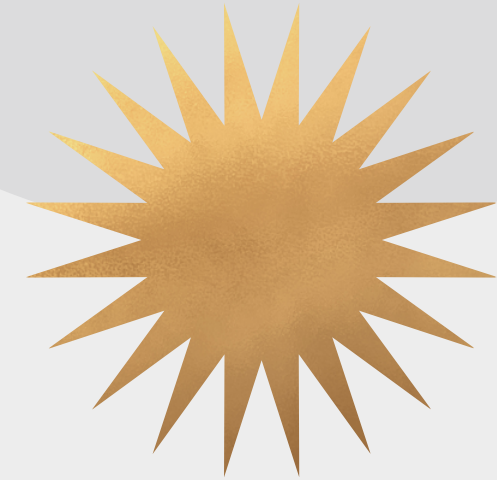
Process-level Risk	Key Control	Design Adequacy
Risk A – Definition (associated process-level objectives)	<ul style="list-style-type: none"><li>● Activity A</li><li>● Activity B</li><li>● Activity C</li></ul>	The indicated key controls are designed adequately to manage this risk to an acceptable level.
Risk B – Definition (associated process-level objectives)	<ul style="list-style-type: none"><li>● Activity A</li><li>● Activity D</li><li>● Activity C</li></ul>	The indicated key controls are <b>not</b> designed adequately to manage this risk to an acceptable level (describe design gap).
Risk C – Definition (associated process-level objectives)	<ul style="list-style-type: none"><li>● Activity E</li><li>● Activity F</li></ul>	The indicated key controls are designed adequately to manage this risk to an acceptable level.



# CREATE A TEST PLAN

# Create a Test Plan

- Determine which controls are important enough to test
  - Are there higher-level controls that might, by themselves, provide reasonable assurance that the relevant risks are managed sufficiently?
  - Are there other compensating controls that address multiple risks?
  - Was the design of controls assessed as being adequate?
  - Have there been changes in the process during the period that result in certain key controls operating for only a portion of the period within scope?

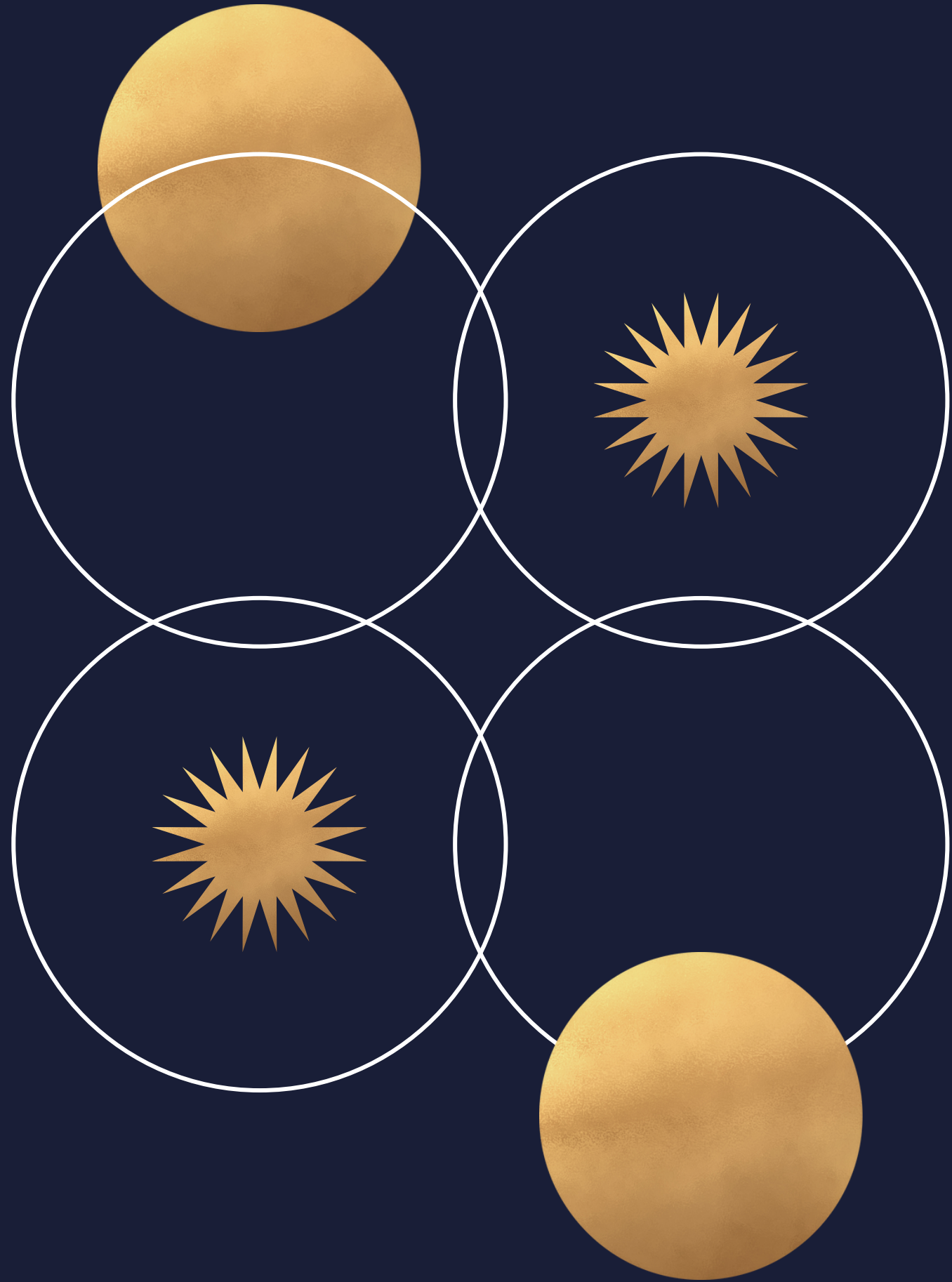


# Create a Test Plan

- Develop an approach for testing those controls
  - Nature of tests
  - Extent of tests
  - Timing of tests
- Document judgments supporting the chosen audit tests.

## EXAMPLE RISK AND CONTROL MATRIX WITH TESTING APPROACH

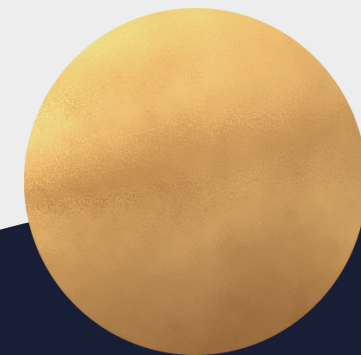
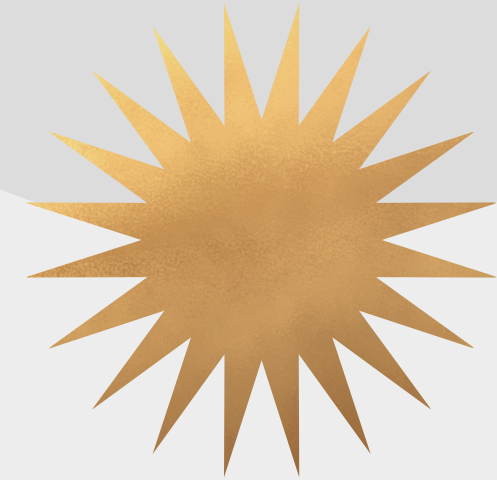
Process-level Risk	Key Control	Testing Approach
Risk A – Definition (associated process-level objectives)	<ul style="list-style-type: none"><li>● Activity A</li><li>● Activity B</li><li>● Activity C</li></ul>	<ul style="list-style-type: none"><li>● Test A</li><li>● Test B</li><li>● Test C</li></ul>
Risk B – Definition (associated process-level objectives)	<ul style="list-style-type: none"><li>● Activity A</li><li>● Activity D</li><li>● Activity E</li></ul>	<ul style="list-style-type: none"><li>● Test A</li><li>● Test D</li><li>● Test E</li></ul>



# DEVELOP A WORK PROGRAM

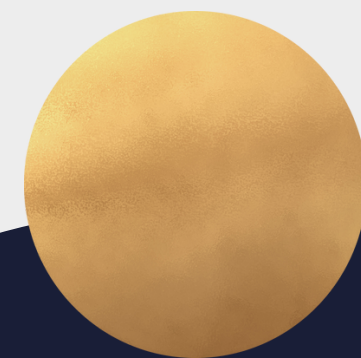
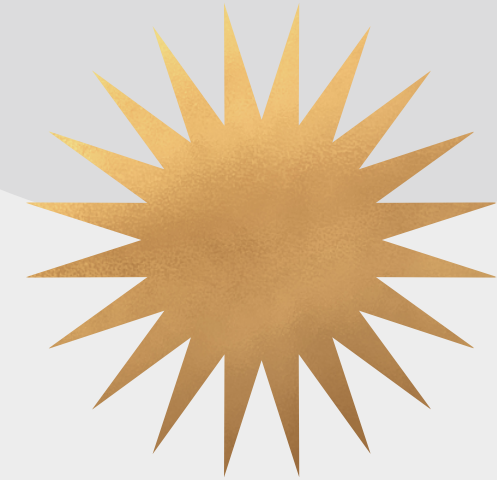
# Develop a Work Program

- Different forms:
  - Standard template or checklist
  - Memorandum summarizing the tasks completed
  - Additional columns in the Risk and Control Matrix
- Format will vary but these are responsibilities emphasized:
  - Ensuring all engagement team members understand what has been done and what still needs to be done.
  - Communicating who is responsible for performing each engagement task.
  - Providing a record of which tasks are completed.
  - Facilitating review by an engagement manager or director who provides oversight and direction during the engagement planning process.



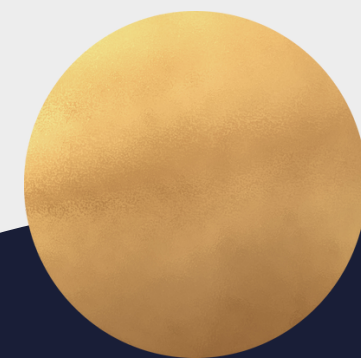
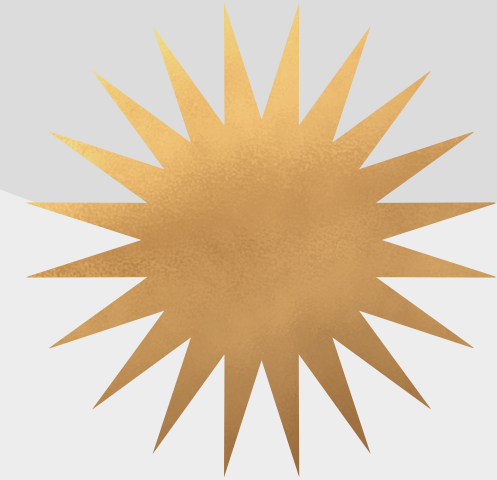
# Develop a Work Program

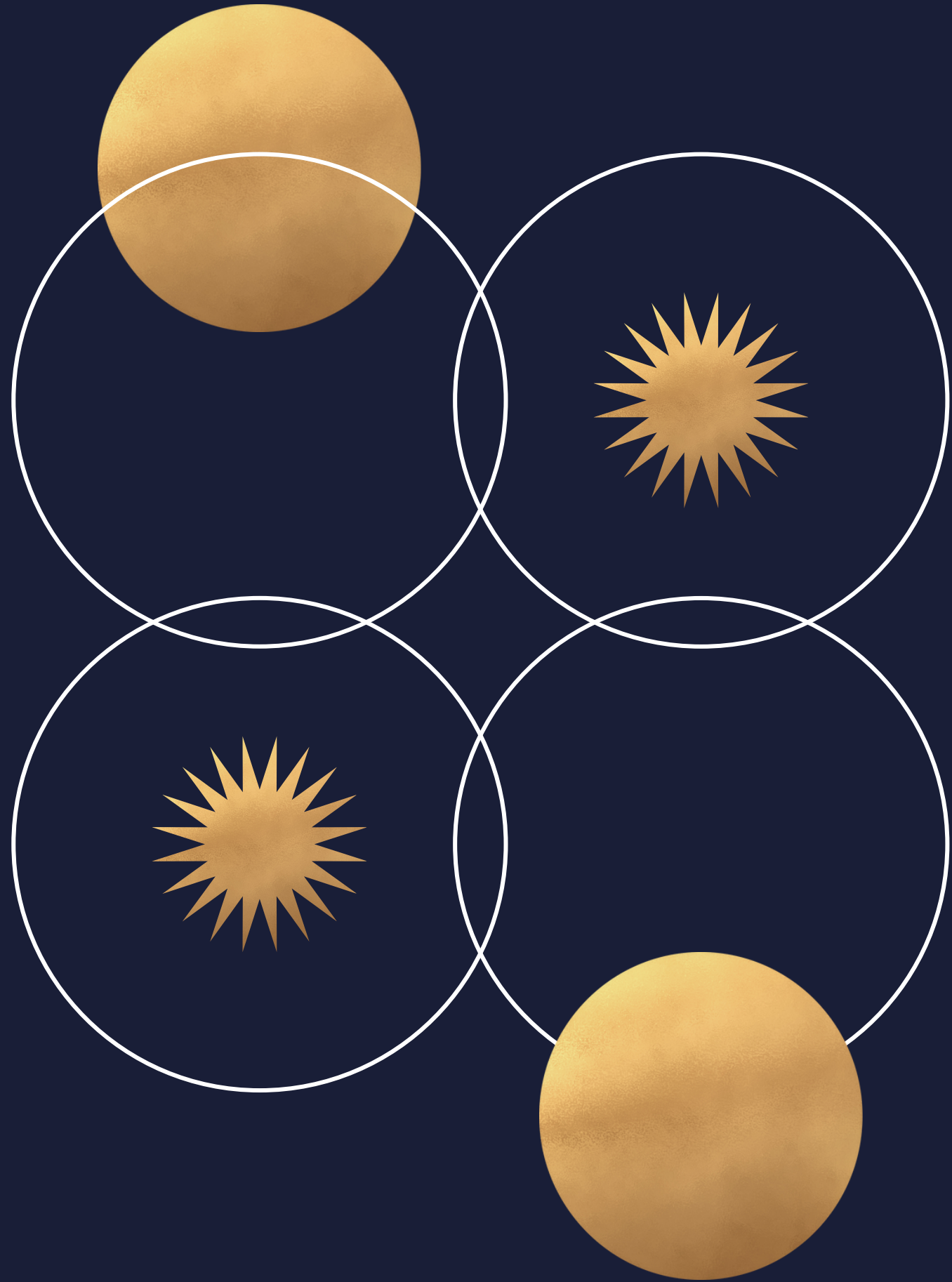
- Elements:
  - Key administrative tasks
  - Key meetings
  - Planning tasks
  - Fieldwork tasks
  - Wrap-up steps
  - Reporting tasks



# Develop a Work Program

- Elements:
  - Key administrative tasks
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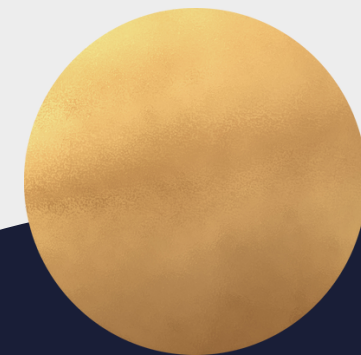
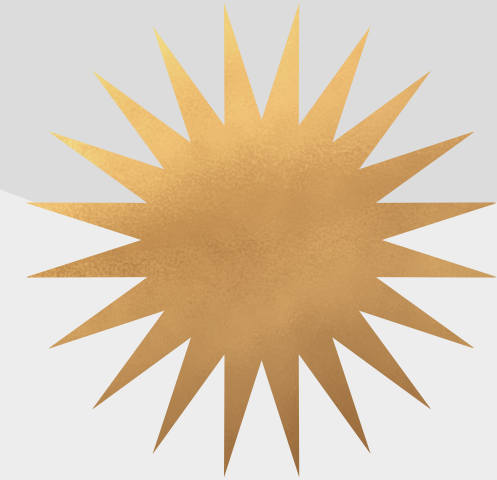




ALLOCATE  
RESOURCES  
TO THE  
ENGAGEMENT

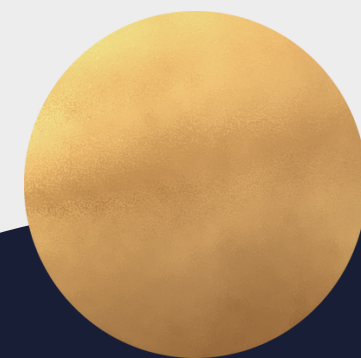
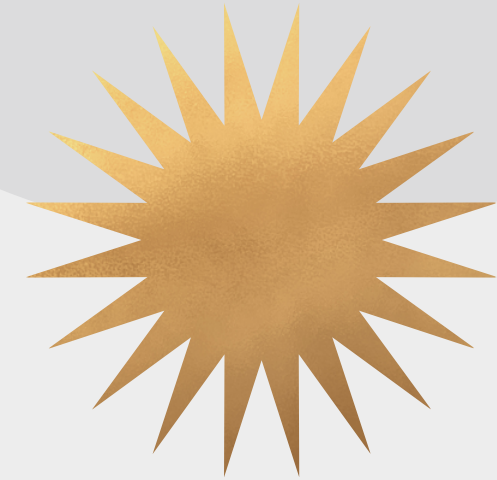
# Allocate Resources to the Engagement

- Engagement Resources
  - Auditors
  - Other people (internal and external)
  - Travel
  - Technology
  - Other
- Budgeting
  - Time
  - Other costs:
    - Travel and related costs
    - Technology costs
    - Supplies



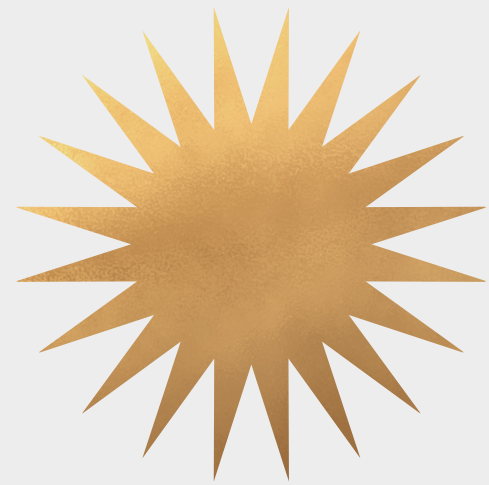
# Allocate Resources to the Engagement

- Allocating Human Resources
  - Skills
  - Previous experience
  - Who has these?
  - Specialty skills not present within the audit function  
(and can they be outsourced at a reasonable cost?)
  - Growth and development of current pool of auditors
  - Unique departmental considerations



# Allocate Resources to the Engagement

- Scheduling
  - Availability of key process personnel
  - Availability of engagement resources
  - Availability of outside resources
  - Availability of key reviewers



# Case Study

**For 15 to 20 minutes, discuss the prelectio case in groups and compare your answers with the recommended contents based on the lecture.**

Process-level Risk	Key Control	Design Adequacy	Testing Approach	Results of Testing	Testing Conclusions
Risk A – Definition (associated process-level objectives)	<ul style="list-style-type: none"> <li>Control A</li> <li>Control B</li> <li>Control C</li> </ul>	The indicated key controls are adequate to manage this risk to an acceptable level.	<ul style="list-style-type: none"> <li>Test A</li> <li>Test B</li> <li>Test C</li> </ul>	<ul style="list-style-type: none"> <li>Result A</li> <li>Result B</li> <li>Result C</li> </ul>	Conclusion covering Risk A
Risk B – Definition (associated process-level objectives)	<ul style="list-style-type: none"> <li>Control A</li> <li>Control D</li> </ul>	The indicated key controls are not adequate to manage this risk to an acceptable level (describe design gap).	<ul style="list-style-type: none"> <li>Test A</li> <li>Test D</li> <li>Test E</li> </ul>	<ul style="list-style-type: none"> <li>Result A</li> <li>Result D</li> <li>Result E</li> </ul>	Conclusion covering Risk B
Risk C – Definition (associated process-level objectives)	<ul style="list-style-type: none"> <li>Control C</li> <li>Control E</li> <li>Control F</li> </ul>	The indicated key controls are adequate to manage this risk to an acceptable level.	<ul style="list-style-type: none"> <li>Test F</li> <li>Test G</li> <li>Test H</li> </ul>	<ul style="list-style-type: none"> <li>Result F</li> <li>Result G</li> <li>Result H</li> </ul>	Conclusion covering Risk C

# THE ASSURANCE ENGAGEMENT PROCESS

## Plan

- Determine engagement objectives and scope.
- Understand the auditee, including auditee objectives and assertions.
- Identify and assess risks.
- Identify key control activities.
- Evaluate adequacy of control design.
- Create a test plan.
- Develop a work program.
- Allocate resources to the engagement.

## Perform

- Conduct tests to gather evidence.
- Evaluate evidence gathered and reach conclusions.
- Develop observations and formulate recommendations.

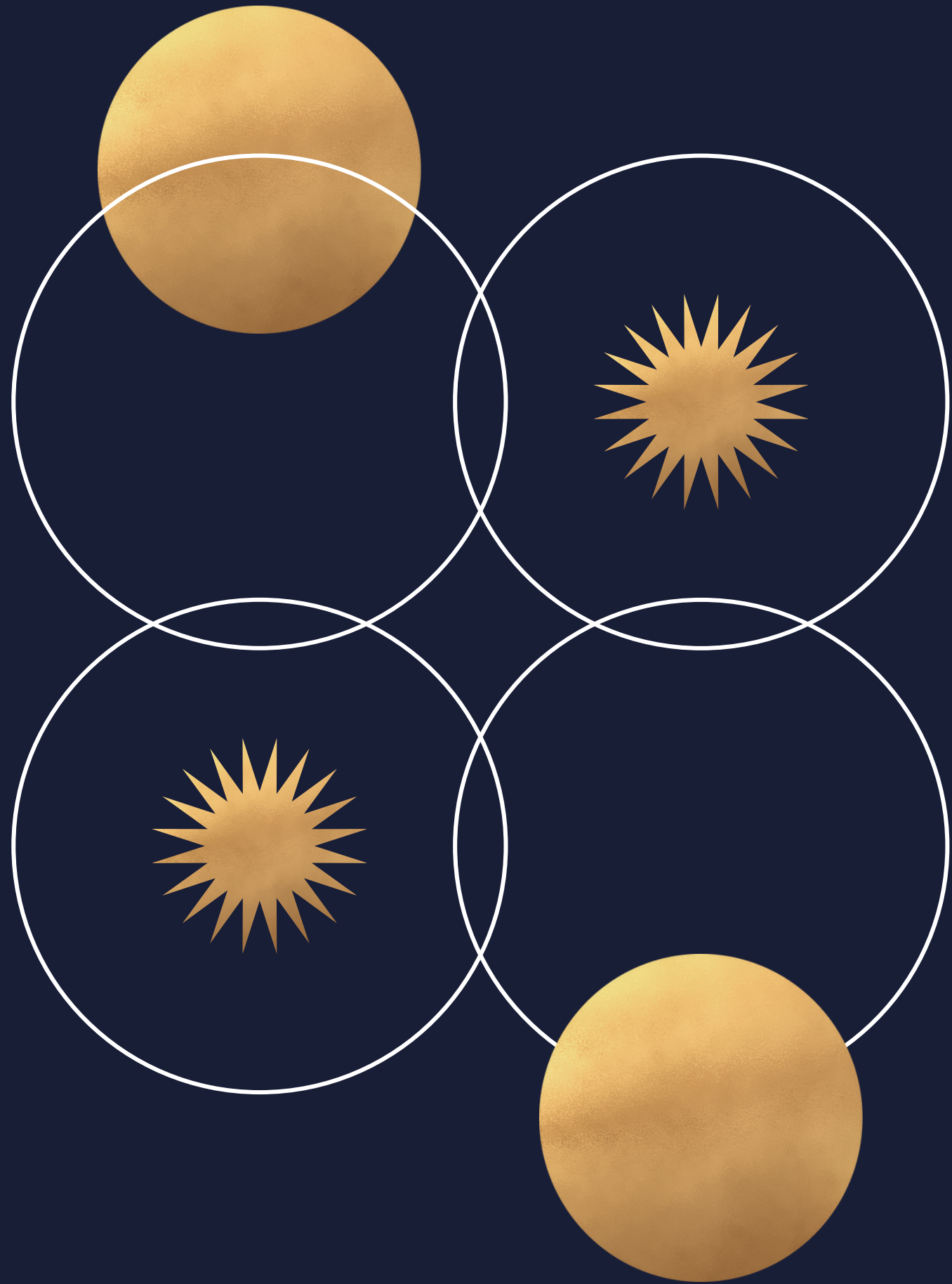
## Communicate

- Perform observation evaluation and escalation process.
- Conduct interim and preliminary engagement communications.
- Develop final engagement communications.
- Distribute formal and informal final communications.
- Perform monitoring and follow-up procedures.



# Performing

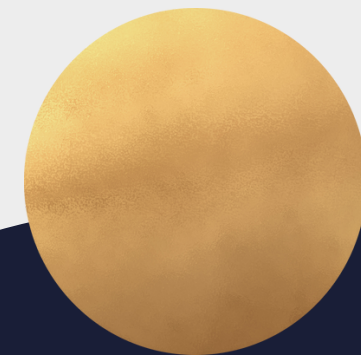
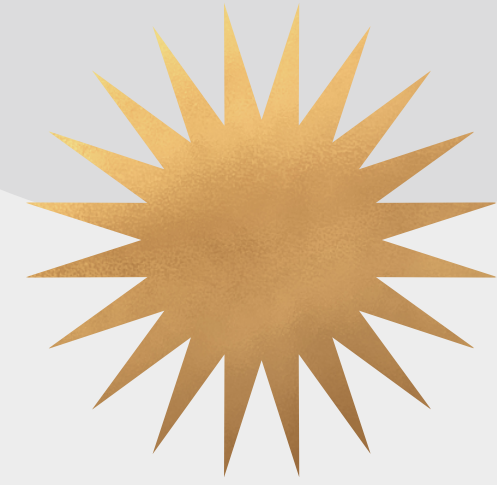
1. Conduct Tests to Gather Evidence
2. Evaluate Evidence Gathered and Reach  
Conclusions
3. Develop Observations and Formulate  
Recommendations



CONDUCT  
TESTS TO  
GATHER  
EVIDENCE

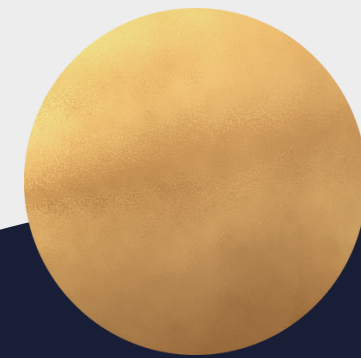
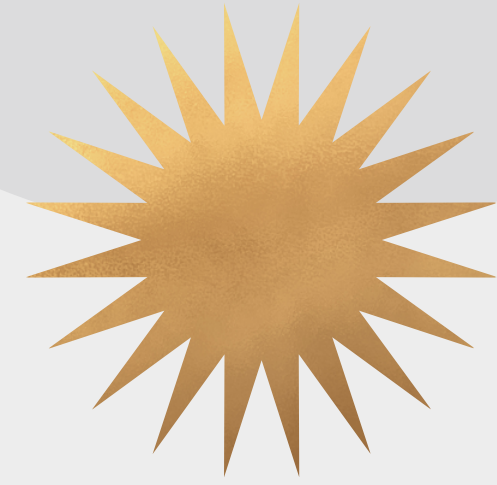
# Conduct Tests to Gather Evidence

- Transition from planning to performing
- Gather evidence
- Additional testing or revise the testing approach



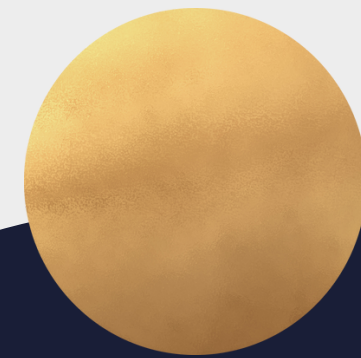
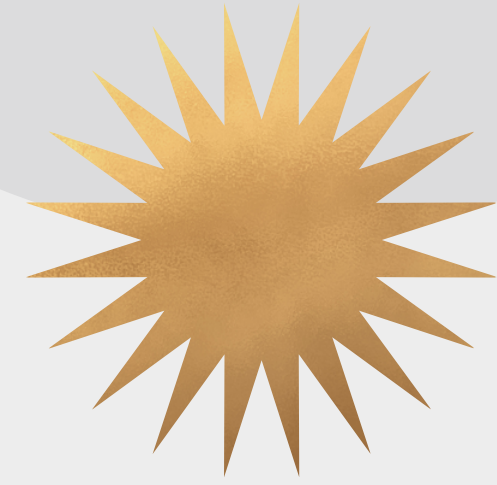
# Evaluate Evidence Gathered and Reach Conclusions

- Are the key controls designed adequately?
- Are the key controls operating effectively, that is, as they are designed to operate?
- Are the underlying risks being mitigated to an acceptable level?
- Overall, do the design and operation of the key controls support achievement of the objectives for the process or area under review?



# Evaluate Evidence Gathered and Reach Conclusions

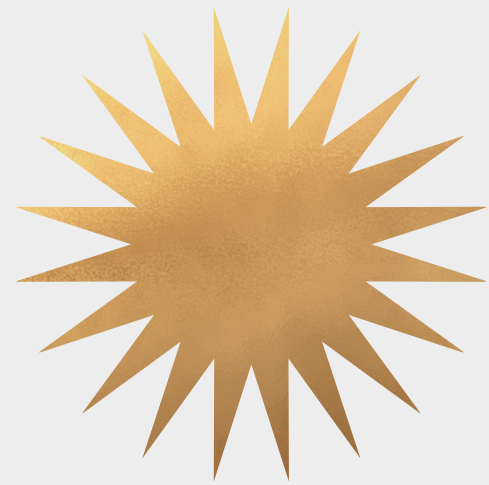
- Are the key controls designed adequately?
- Are the key controls operating effectively, that is, as they are designed to operate?
- Are the underlying risks being mitigated to an acceptable level?
- Overall, do the design and operation of the key controls support achievement of the objectives for the process or area under review?



# Develop Observations and Formulate Recommendations

- Finally, any control deficiencies identified during the engagement should be documented to facilitate discussion with appropriate management and, ultimately, communication to appropriate stakeholders

Process-level Risk	Key Control	Design Adequacy	Testing Approach	Results of Testing	Testing Conclusions
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Risk C – Definition (associated process-level objectives)	<ul style="list-style-type: none"> <li>Control C</li> <li>Control E</li> <li>Control F</li> </ul>	The indicated key controls are adequate to manage this risk to an acceptable level.	<ul style="list-style-type: none"> <li>Test F</li> <li>Test G</li> <li>Test H</li> </ul>	<ul style="list-style-type: none"> <li>Result F</li> <li>Result G</li> <li>Result H</li> </ul>	Conclusion covering Risk C

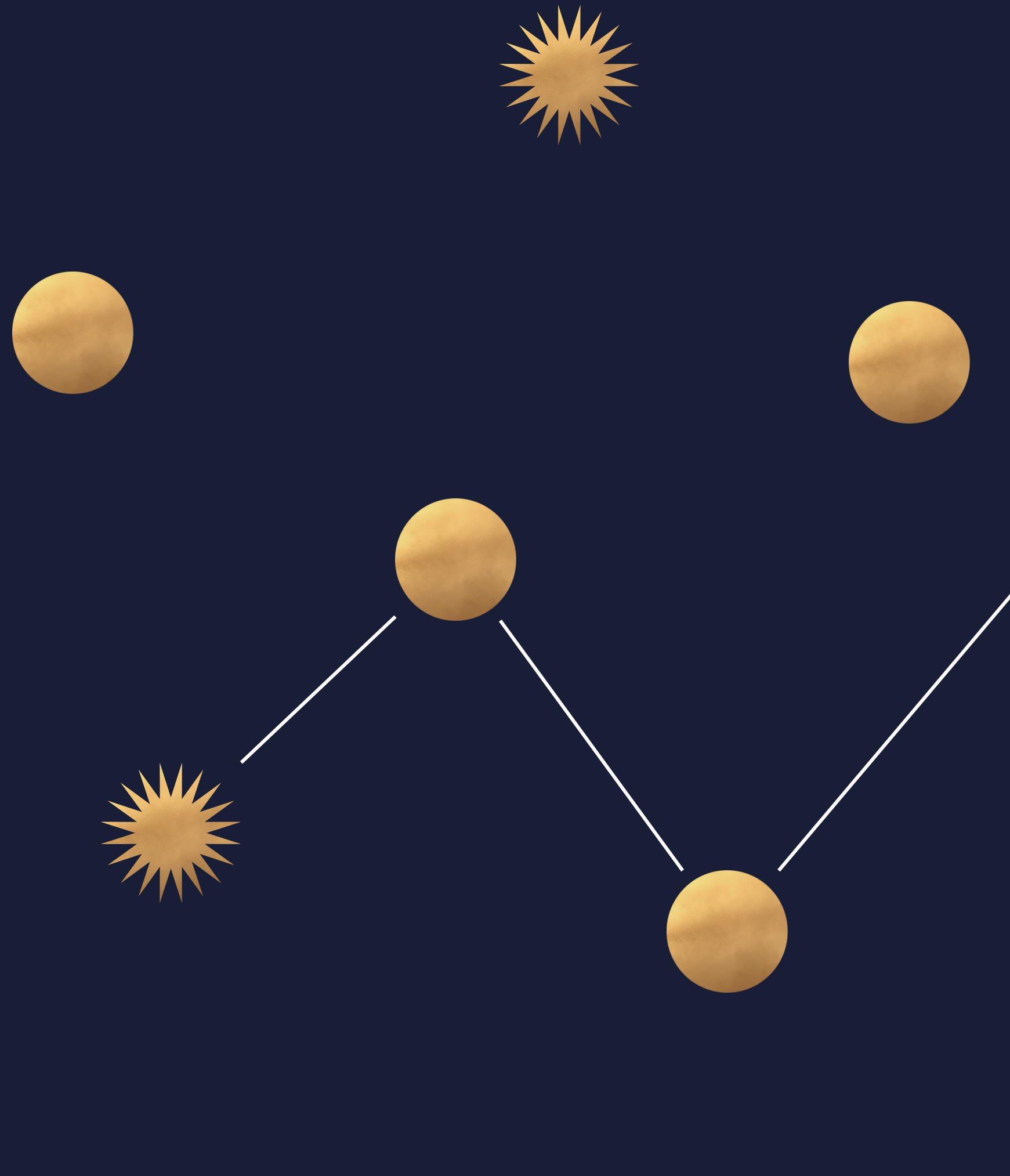


# Case Study

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## Next Meeting:

- Communicating Assurance Engagement Outcomes and Performing Follow-Up Procedures



Thank you!

