

Internal Auditing

Financial Control Review - The product

DETAILED AUDIT PROGRAM

Subsidiary, Division or Location	ABC Co. Somewhere USA
Audit Date	November 17, xxxx - November 21, xxxx

Prepared or Updated by	Date	Reviewed by	Date
J. Doe	11/6/XX		

Engagement Team Members	Sign-off
J. Doe	
J. Smith	
B. Brown	

PROCEDURE

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DOCUMENTATION OF WORK PERFORMED

General Reporting

Detail Tests

1. Obtain the MS Copylot feeds into MISCON from management, for the September month-end close. Also obtain the Company wide MIS Reporting Standards which identify which trial balance accounts point to which financial statement line on the balance sheet and P&L and ensure all accounts are pointed to the correct financial statement line.
2. Using the same month-end close, trace the trial balance accounts to the month-end “strip” submitted to the XYZ for the September month-end close.
3. Coordinate with Ms. X, in the XYZ, how the strip submitted by Consumer Care for the September month-end close, ties into the Corporate Consolidation submitted to country. Keep on file for future testing during the XYZ December 15, xxxx audit.

Note: During the XYZ December 15 audit, IA will agree divisional “feeds” into the Corporate consolidation to ensure the “Divisional” trial balance is equal to the “Corporate” trial balance, with the exceptions of journals booked at Corporate.

4. In connection with the review of the MISCON submitted to the XYZ, also understand what other “non-financial” key data is submitted with the MISCON reporting (ie headcount, # of lbs of certain product produced, etc.) and review the source of that data. On a test basis, select different months, and determine whether a consistent data source was used each month. Inquire of management as to whether this is the most “appropriate” source for the requested information.

Inquiry Procedures

5. Inquire of local management as to whether any responsibility centers not grouped differently from SAP to DRGS during the

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<p>NOTE: Arthur Andersen is performing a review of the cash accounts during their review of the XYZ, therefore all cash procedures are excluded from this audit program.</p>				
<p><u>Accounts Receivable</u></p> <p>1. <u>Detail Tests</u></p> <p>a. Select 5 Accounts Receivable reconciliations to test. Ensure selection is representative of the period January 1, xxxx - September 30, xxxx. Include the September month-end reconciliation in the selection. For the 5 account reconciliations selected, perform the following:</p> <ol style="list-style-type: none"> 1. Agree the general ledger balance per the reconciliation to the Accounts Receivable balance per the SAP general ledger. 2. Test the clerical accuracy of the account reconciliation. 3. Discuss significant reconciling items with management. Determine if the division is experiencing problems reconciling the two, based on the volume and magnitude of items noted. 				
<p>2. Obtain examples of SAP exception reports for Accounts Receivable, Accounts Payable and Inventory. Review the related exception reports. Determine whether the exception reports are functioning as designed and whether management is following up on the appropriate items on a timely basis. Select several different days to test.</p>				
<p>NOTE: External Audit FIRM CCC is reviewing the adequacy of the Accounts Receivable Balance and related Allowance for Doubtful Accounts during their review of the XYZ, thus explaining why the majority of the typical A/R procedures are excluded from this audit program.</p>				

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<p><u>Inventories</u></p> <p><u>Minimum Procedures</u></p> <p>1. <u>Analytical Procedures</u></p> <p>a. Compare the current year inventory balances with the balances at December 31, XXXX, to budgeted amounts, and to expected balances based on current operations. Investigate significant fluctuations (> \$500,000).</p>				
<p>2. <u>Detail Tests</u></p> <p>a. Obtain inventory reconciliations for significant inventory accounts as of September 30, xxxx. Trace the general ledger balance per the reconciliations to the general ledger balance per SAP. Test the reconciliations for clerical accuracy. Review reconciling items for appropriateness.</p> <p>b. Discuss significant reconciling items with management.</p> <p>3. Obtain client's calculation of the obsolescence reserve as of 9/30/XX. Understand information used to prepare the calculation and agree to supporting reports (ie aging reports) where applicable. Consider the adequacy of the reserve given levels of inventory built up in comparison to forecasted sales and new product lines (ie will any existing product lines become obsolete as a result of the new lines launched). Compare to results obtained from the review of inventory turns and gross margins by product lines.</p>				

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<p>4. <u>Inquiry Procedures</u></p> <p>Make and document the results of the following inquiries:</p> <ol style="list-style-type: none"> a. The client's procedures for accounting for "in-transit" inventory. Inquire as to whether these procedures are consistently applied. Review supporting documentation. b. The client's procedures for accounting for cut-off of purchases and shipments at month-end. c. The client's procedures for accounting for returned goods. d. The client's procedures for accounting for consignment stock. e. The client's procedures for accounting for outside processors. f. The client's procedures for monitoring purchase price variances and other related inventory variances. Analytically review such variances as of September 30, xxxx. 				
<p>5. The client's procedures for determining and adjusting for obsolete items or items in excess of net realizable value, that such a determination was made and whether inventory valuation reserves, if any, are considered by the client to be adequate. Also, inquire whether these procedures have been consistently applied in accordance with Company policy.</p>				
<p>6. Review inventory statistics between periods and inquire about significant fluctuations in the following:</p> <ul style="list-style-type: none"> - Inventory turnover - Gross margin percentages 				
<p>NOTE: Arthur Andersen will observe physical inventories and review the related book-to-physical adjustments.</p>				

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<p><u>Prepaid Expenses</u></p> <p><u>Minimum Procedures</u></p> <p>1. <u>Analytical Procedures</u></p> <p>a. Compare the current year prepaid expense with the balance at December 31, XXXX and to the expected balance based on current operations. Investigate significant fluctuations. Review supporting detail for any balances > \$500,000.</p> <p>b. Relate changes in prepaid expense accounts to changes in the related income/expense accounts if deemed necessary.</p>				
<p><u>Property, Depreciation and Capital Leases</u></p> <p><u>Minimum Procedures</u></p> <p>1. <u>Analytical Procedures</u></p> <p>a. Compare the September 30, xxxx balances in the property accounts with the balances at December 31, XXXX, to budgeted amounts, and to expected balances based on current operations. Investigate significant fluctuations.</p>				
<p>b. Analyze change in depreciation expense between periods, taking into account asset additions, retirements and depreciation methods. Relate depreciation expense to changes in the related income/expense accounts. Compute depreciation expense as a % of PP&E costs, by fixed asset classifications, to determine reasonableness of depreciation expense.</p>				

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<p>2. <u>Inquiry Procedures</u></p> <p>Make and document the results of the following inquiries:</p> <p>a. Reasons for significant variations in property account balances.</p>				
<p>b. The client's policies for the capitalization of fixed assets. Specifically inquire of the procedures used to monitor when assets are first depreciated (ie what is the review process used to ensure that assets ready for their intended use, are depreciated on a timely basis). Review CIP balances to understand if this is a potential issue. Investigate as deemed necessary.</p>				
<p>c. Whether all property retirements/disposals have been properly accounted for.</p>				
<p>d. The client's procedures for determining depreciation lives and methods, whether such determination is consistent between periods and whether property account balances are not in excess of net realizable value.</p>				
<p>3. <u>Detail Tests</u></p> <p>a. Obtain a fixed asset reconciliation as of September 30, xxxx which agrees the balances per the fixed asset system to the general ledger. Investigate significant reconciling items. Clerically test the summary.</p>				

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<u>Additional Procedures (as deemed necessary)</u>				
4. Review a listing of property additions to ensure that all items have been capitalized in accordance with the client's capitalization policy on a timely basis. Test additions > \$500,000.				
5. Review a schedule of property retirements to determine that gains/losses have been properly accounted for, if deemed significant.				
6. Have the client perform (or perform) a lease capitalization test for all significant new leases, including summarizing appropriate financial statement disclosures.				

<u>Other Assets</u>				
<u>Minimum Procedures</u>				
1. <u>Analytical Procedures</u>				
a. Compare the Other Assets balances as of September 30, xxxx with the balances at December 31, XXXX and to expected balances based on current operations. Investigate significant fluctuations. Obtain detail support and relate change to related income/expense accounts, if deemed necessary.				
b. Consider the client's procedures for determining the realizability and classification of other assets, that such a determination was made, and that other assets are properly classified in the financial statements.				

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<p><u>Accounts Payable</u></p> <p><u>Minimum Procedures</u></p> <p>1. <u>Analytical Procedures</u></p> <p>a. Compare the accounts payable balance as of September 30, xxxx with the balance at December 31, XXXX and to expected balance based on current operations. Investigate significant fluctuations.</p>				
<p>2. <u>Inquiry Procedures</u></p> <p>Make and document the results of the following inquiries:</p> <p>a. The client's procedures to ensure proper accounts payable cutoff at year-end and that all payables are recorded as of the balance sheet date. Coordinate with the A/P contact at the XYZ. Refer to step #3b below for the search for unrecorded liabilities.</p>				
<p>3. <u>Detail Tests</u></p> <p>a. Obtain an Accounts Payable reconciliation as of September 30, xxxx, and agree the accounts payable trial balance (sub-ledger) to the general ledger balance per SAP. Clerically test the reconciliation. Investigate significant reconciling items. Discuss significant items with management.</p> <p>b. In connection with step #2a above, perform a search for unrecorded liabilities for payments > \$250,000 subsequent to September 30, xxxx. Determine if product/service was recorded in the appropriate period.</p>				
<p><u>Additional Procedures (as deemed necessary)</u></p>				

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4. Review the detail accounts payable listings for large/ unusual items or amounts (e.g., related-party amounts). Make inquiries of the client as necessary.				
<p><u>Intercompany</u></p> <p><u>Minimum Procedures</u></p> <p>1. <u>Detail Tests</u></p> <p>a. Obtain a listing of the intercompany account balances as of September 30, xxxx. Agree listing to the trial balance. Inquire of management how these balances are confirmed with other divisions. Confirm the balances agree with the respective affiliate by either 1) sending faxes to the respective affiliate company to confirm the balance or 2) liaise with personnel at the XYZ to confirm the amounts booked on the respective affiliate company books.</p>				

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<p><u>Accrued Expenses</u></p> <p><u>Minimum Procedures</u></p> <p>1. <u>Analytical Procedures</u></p> <p>a. Compare the September 30, xxxx accrued expense balances with the balances at December 31, XXXX and to expected balances based on current operations. Investigate significant fluctuations > \$500,000. Specifically investigate accrued balances for shipments made but not billed (the cost of goods sold clearing a/c).</p>				
<p>b. Relate changes in significant accrued expense balances to changes in the related income/expense accounts.</p>				
<p>2. <u>Inquiry Procedures</u> - Make and document the results of the following inquiries:</p> <p>a. Reasons for significant variations in accrued expenses balances between periods.</p>				
<p>b. The need for additional accrued expenses not already reflected in the financial statements, including the following:</p> <ul style="list-style-type: none"> ■ Payroll and payroll taxes ■ Vacation/holiday pay ■ Pension and/or profit sharing ■ Bonus ■ Warranty ■ Post-retirement employee benefits ■ Reserves for self-insured claims ■ Other 				

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<p>3. <u>Detail Tests</u></p> <p>a. For the accrued expenses account balances > \$500,000, understand how the balance was computed and agree to supporting documentation.</p> <p>b. Based on the results obtained in #1a, if deemed necessary, perform detail tests of the COGS clearing account by reviewing a client-prepared reconciliation of the account, plus tracing detail transactions to warehouse documentation, on a test basis. Inquire of Sales support representatives whether they are reviewing order reports for past due orders and items shipped but not invoiced (the ZSOPNPAS Report and the Billing Due List). Review recent copies of these reports.</p> <p>c. Obtain a detail understanding of how general ledger entries are recorded in this clearing account and how the entries are cleared out of this account.</p>				
<p><u>Reserves</u> The The product division has reserved for restructuring charges, the disposal of the XYZ business and an FDA initiative (industry coalition agreement). External Audit Firm CCC will review the disposal of the XYZ business and the restructuring accrual.</p> <p><u>Minimum Procedures</u></p> <p>1. <u>Analytical Procedures</u></p> <p>a. Compare the reserve balance at September 30, xxxx with the balance in at December 31, XXXX and discuss significant variations with management.</p>				

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<p>2. <u>Detail Tests</u></p> <p>a. Obtain a progression of the Restructuring reserves as of September 30, xxxx which identifies movements/activity from December 31, XXXX through September 30, xxxx. Agree ending balances to the general ledger. Provide workpaper to Arthur Andersen for Arthur Andersen to do further testing.</p> <p>b. Determine if the reserve is adequate and not excessive by comparing to estimated and probable charges, by inquiring of management and by liaising with the auditors conducting the remediation reserves.</p> <p>c. Obtain an understanding of the Reserve for FDA initiatives (ie A/C G60825 Project Deposit) via inquiries of .Document accordingly. Also obtain a progression of the account activity from December 31, XXXX through September 30, xxxx. Determine adequacy of reserve as of September 30, xxxx.</p>				
<p><u>Other Liabilities</u></p> <p><u>Minimum Procedures</u></p> <p>1. <u>Analytical Procedures</u></p> <p>a. Compare the other liabilities balance as of September 30, xxxx with the balance at December 31, XXXX and to expected balance based on current operations. Investigate significant fluctuations > \$ 500,000.</p> <p>b. Relate changes in significant other liabilities balance to changes in related income/expense accounts.</p>				

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<p>2. <u>Inquiry Procedures</u></p> <p>Make and document the results of the following inquiries:</p> <p>a. Reasons for significant variations in other liabilities account balances.</p>				
<p>b. The client's procedures for determining the classification of other liabilities, that such a determination was made, and whether other liabilities are properly classified in the financial statements.</p>				
<p><u>Additional Procedures (as deemed necessary)</u></p>				
<p>3. Review a detail list of other liabilities for unusual items or amounts. Make inquiries of the client as necessary.</p>				
<p><u>Subsequent Events & Transactions, Commitments</u></p> <p><u>Minimum Procedures</u></p> <p>1. <u>Inquiry Procedures</u></p> <p>Make and document the results of the following inquiries:</p> <p>a. If there have been any events, or transactions that occurred after September 30, xxxx that have a significant effect on the financial statements or should be disclosed therein.</p>				

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<p><u>Additional Procedure (As deemed necessary)</u></p> <p>2. Inquire as to any material contractual obligations for the construction or purchase of assets and consider for footnote disclosure.</p>				
<p><u>Profit and Loss (Operations Review)</u></p> <p><u>Minimum procedures</u></p> <p>1. <u>Analytical Procedures</u></p> <p>a. Compare revenue and expense account balances with those of the prior year (or to budgeted amounts) and to expected balances based on current operations. Specific accounts/amounts to review would ordinarily include:</p> <ul style="list-style-type: none"> - Sales (Revenue) - Cost of sales - Gross margin - Selling and administrative expenses - Other income and expense 				
<p>b. Cross reference revenue and expense balances, where applicable, to analyses of balance sheet accounts (e.g., depreciation expense to property).</p>				

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<p>2. <u>Inquiry Procedures</u></p> <p>Make and document the results of the following inquiries:</p> <p>a. Reasons for significant variations in revenue and expense account balances (Note: a client-prepared operations memo may be reviewed in lieu of making specific inquiries). Relate the responses to our inquiries to our understanding of the client's business, particularly changes in operations during the year, changes in accounting principles and the results of our work on the balance sheet accounts.</p>				
<p><u>Additional Procedures (as necessary)</u></p> <p>1. Inquire as to whether the revenue and expense account balances have been properly classified for financial reporting purposes on a basis consistent with the prior period. Inquire of any policy changes with respect to revenue and expense accounts.</p>				
<p>2. Inquire as to whether the financial statements need to reflect discontinued operations or extraordinary/unusual item treatment of revenue and expense accounts.</p>				

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<p><u>Financial Statement Close Process</u></p> <p>1. <u>Inquiry Procedures</u></p> <p>a. Obtain an understanding of the financial statement close process via inquiries of management. Inquire of the following:</p> <ul style="list-style-type: none"> ■ What is performed each day during the month-end close (ie Day 1, Accountant 1 performs a tie-out of X account to the g/l. Day 2 Accountant 2 performs an analytical review of the balance sheet accounts, Day 3....). Concentrate on identifying control weaknesses and potential efficiencies in the process. ■ What kind of support is attached to journal entries, particularly for the Reserve accounts. Determine adequacy of documentation. ■ Determine if procedures are different for the quarter month-ends. Document the differences. ■ For recurring journal entries, determine if source documents/references are evaluated for reasonableness each month-end. ■ Determine if journal vouchers are approved by management. Select a few journal vouchers to test throughout the year in order to verify if the Company policy/procedure is followed (assuming this is Company policy). If it is not Company policy to do so, consider recommendation for audit report. 				
<p><u>Follow up to the Internal Audit Report issued in XXXX</u></p> <p>1. Review the Internal Audit Report issued in XXXX for the Consumer Care Division. Discuss status of action points that management agreed to in the report. Document accordingly.</p>				

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