

I. Pre-Audit Preparation

1. Define the Purpose of the audit.
2. Define the Objectives of the audit.
3. Define the Scope of the audit.
4. Conduct a brief and informal question and answer session with department supervisor to determine if there have been any material changes in operations since the last audit. If there has been a material change, prepare a new Procedural Narrative for the permanent file.
5. If the scope of the audit is unusually large, or if the anticipated man-hours allotted for this audit is projected to take longer than 10 business days, an Information and Documentation Request form will be sent to the department manager giving them two weeks to gather all documentation necessary to perform the audit. (See standard Information and Documentation Request form in appendix).

II. Establishing the Scope of the Audit

1. Determine if this is an existent audit workprogram. If yes, go to #2. If no, go to #3.
2. Review workprogram and determine if there have been any material changes that would warrant revising the workprogram:
 - A. Have there been any changes in internal procedures?
 - B. Has personnel been reduced in the area which could compromise dual controls?
 - C. Have there been any regulatory updates that warrant review?
 - D. Have any processes become automated?
3. Create a workprogram for function to be audited.
 - A. Review any published regulation or law and address all requirements.
 - B. Incorporate internal processing procedures
 - i. System Input/Output
 - ii. Written policies/procedures
 - iii. Secondary reviews/authorizations
4. Develop an Internal Control Questionnaire if appropriate
 - A. Substantially all questions should be answered with a YES/NO/NA

III. Conducting the Audit

1. Determine if Positive or Negative confirmations are applicable to the audit work conducted. Prepare confirmations for delivery.
2. Determine the sampling method to be used for the audit. (See appendix for definitions of various sampling methods).
3. Determine the type of reports needed to conduct the audit. Those typically best suited for audits are: independent trial balances, summaries, exception listings, confirmation listings, analytical reports, management reports, and internal audit administrative reports.
4. Preparing workpapers. The work papers should tell a complete story of the work performed. It is imperative that the record left by the auditor of the work that was performed and the conclusions reached is clear and defensible. The following represents the way workpapers should be created:
 - A. The work papers must document the scope of the work performed. This will include the audit program, the percentage of items in the population that were tested, statistical sampling techniques used, the inquiries made, the confirmations mailed and received, etc. The work papers must clearly support the amount of testing that was undertaken was sufficient under the circumstances.
 - B. The results of the audit test should be clear. This will include all of the audit exception items and their resolution, the documents and document attributes examined, the reconciliations performed, etc. This documents that all of the procedures in the audit program were indeed performed.
 - C. It should be made clear the link between any conclusion derived and the evidence obtained. All of the judgements and interpretations made during the course of an audit should be in the work papers and should be solidly based on the evidence gathered.
 - D. Tickmarks should always be used consistently throughout the entire audit. No tickmark should have more than one meaning at any time.

IV. Preparing the Audit Report

1. Prepare an Excel spreadsheet of all audit findings. Fields should include: Workpaper reference Number, Section, ON/OFF report indicator, and a Comments Section. The Comments Section is where the actual audit finding will be described.
2. Draft a Preliminary Report of all audit findings and audit recommendations. This report should be discussed with the Department Manager and corrective actions should be addressed at this time. The benefit of preparing a Preliminary Report is to allow the Department Manager to defend itself against any findings. There may be a reasonable explanation for any finding. However, additional documentation should be obtained before removing any exception from the Final Audit Report. This provides an evidentiary trail to back up the Department Manager's position. Any exception to this requirement should be brought to the attention of the Internal Auditor before the Final Audit Report is written. All Preliminary Reports should be indicated as such by stamping "Tentative and Preliminary, Not For Distribution" to all pages of the report. This will also be indicated on the audit findings report in the "Status of Finding" field.
3. The Final Audit Report should be prepared in accordance with the sample format attached. It will be the policy of this department to obtain uniformity when writing all audit reports. Each audit report should include:
 - A. The Purpose of the audit
 - B. The Objective of the audit
 - C. The Scope of the audit
 - D. The sampling technique involved
 - E. Time frame in which the audit was conducted
 - F. Description of audit procedures applied to testwork
 - G. Assign a "PRIORITY" rating – LOW/MODERATE/HIGH – This directly correlates to the associated risk.
 - H. State the "Status of Finding" – PRELIMINARY or FINAL.
 - I. Audit exception with the associated risk
 - J. Audit recommendation
 - K. Corrective action taken. This is indicated in the audit report as the "Action Plan".
4. Any Corrective Action taken must be completed prior to writing the Final Audit Report. This demonstrates an agreement to each finding and facilitates corrective action. The Internal Auditor must approve any exception.
5. Audit reports should be written in the active language, be impersonal, and be written in a positive fashion. The Final Audit Report must express an opinion of the adequacy, effectiveness, and efficiency of the control system and the quality of ongoing operations. When making a recommendation for a corrective action in the report, a comment must be made on the potential exposures that exist if the corrective action is not taken. For example, certain regulatory violations could lead to Civil Money Penalties (CMPs) not only for the bank, but also for individual employees.
6. For audits with an unusually high number of findings or for findings that are deemed to be in a high-risk area, a time should be stated for an audit follow-up to ensure corrective actions have been fully implemented.

Basic Audit Definitions

Positive Confirmations – Request a response regardless of the circumstances. Positive Confirmations are best suited for high balance, low volume assets accounts, especially when there may be a question of fictitious or overvalued assets. Remember though, these types of confirmations require more time to ensure a response is received, a non-response is almost treated as an exception itself.

Negative Confirmations - Request a response only if there is a discrepancy between the customer's records and the bank's balances. Negative Confirmations are best suited for low balance asset or liability accounts.

Evidential matter – the underlying accounting data and all corroborating information available to the auditor. Evidence is basically what the auditor gathers through examination of the accounting records, interviews, observation, tests, and analytical review.

Sufficient evidence – means that enough evidence is assembled to assure that audit conclusions are well founded.

Competent evidence – means relevant, valid, and convincing. Both the substance and the interrelationship of evidence demonstrate competent.

Direct evidence – evidence obtained by observation or inspection, is considered to be more reliable than indirect evidence, such as that obtained by confirmation and inquiry.

Population – All of the records of a given type that are under review. (I.e. All installment loans, all active Certificates of Deposit, etc.)

Sample – A portion of the records in the population chosen for review.

Random Sample – A sample of the records in a population chosen by chance procedures and giving all items in the population an equal chance of being included in the sample.

Judgement Sampling – A sampling method that allows the auditor to choose the items from the population to be sampled. The advantage to this approach is the use of the auditor's insight into vulnerable areas in the population.

Stratified Random Sampling – This sampling method is used when a population is not homogeneous. The audit risk results from a combination of the existence of material errors and the failure to detect these errors. Stratification allows for the identity of groups of the population that allows the auditor to sample those areas of greatest perceived risk.

Cluster Sampling – This sampling method is used to select a required sample size by taking an arbitrary random sampling points and taking cluster items to be sampled.

Monetary-Unit Sampling – This sampling method is a statistical method in which every dollar in the population is given an equal chance of selection. This is done by changing the customary definition of sampling unit from an individual invoice or an individual receivable balance to being an individual dollar.

Test data – (For auditing computer procedures) – Using test data, special transactions are prepared and are processed under the bank's normal applications, and the actual results are compared with the expected results. The method is useful in testing input controls, error detection controls, transaction validation routines, processing logical and file maintenance and update procedures.

Audit trail – The auditor recreates transactions completely by following the trail of evidence that the transaction left through the paper accounting and bookkeeping systems. Note: With the increased use of computer generated entries, this "paper trail" is not always available. Audit procedures will have to be modified to adapt to computer generated entries.

Input Controls - These controls are designed to provide reasonable assurance that authorized data is properly entered into the system. These input controls may be a part of the system's software, such as control totals on input reports or may be generated externally, such as a batch-control log. For on-line systems the input control often consists of a password restriction which allows only authorized individuals to access the system.

Processing Controls – These controls are designed to provide reasonable assurance that authorized transactions are correctly processed and data files are properly updated and protected. Typical processing controls are application edit procedures that verify the accuracy of data.

Output Controls – These controls are designed to provide assurance that output is reasonable and only made available to authorized users. Typical output controls include reconciliations by authorized users with input and processing control totals.

Cost/Benefit Analysis – The cost of controls should never exceed the benefit derived.

Segregation of Duties – The basic idea behind segregation of duties is to organize the work to be done in such a way as to prevent a single individual from being able to both perpetrate and conceal an irregular transaction. People that have access to assets should not have access to the accounting records. People that make entries to the accounting records should not perform period-ending reconciliations.

Access Controls – These are really a subset of the segregation of duties concept. The control system should ensure that only those who need access to assets have it. This is especially true for highly liquid assets such as cash, official checks, etc.

Dual Custody – The concept that it requires two or more individuals to access the assets. For example, this would be applicable to the opening of night deposit bags, packaging currency shipments, and the opening of currency and collateral vaults. However, when a single employee is responsible for the custody of an asset and is individually accountable for it, then dual custody is not appropriate. I.e. Tellers individual cash drawer.

Internal Control Questionnaire – A series of highly specific and detailed questions in the form of a checklist about the operations under review. The questions are usually structured in a way that call for a simple, “yes”, “no”, or “not applicable”.

Flowcharts – A flowchart is a visual representation of the flow of information and documents in an area under review. Symbols representing documents, processes, operations, and files are linked by arrows or lines depicting the flow of paper and data from the point of entry to the system to the point of exit from it. Flowcharts are useful because of the graphic and visual way the working of a system are represented.

Procedural Narratives – The concept is simple, but the competent execution may be one of the most difficult tasks facing the auditor in the entire audit process. The auditor simply sits down with the people doing the work and takes notes as they tell him what they do, and to the best of their abilities, why they do it. Based on these discussions, and review of the appropriate documentation, the auditor writes down what he knows of how the system is supposed to work.

Significant Audit Findings – Audit findings that are those conditions which, in judgment of the Internal Auditor, could adversely affect the organization. Significant audit findings may include conditions dealing with irregularities, illegal acts, errors, inefficiency, waste, ineffectiveness, conflicts of interest, and control weaknesses.