

Test of internal enterprise controls

Motivation. While dealing with internal controls at the enterprise during external audit engagement, complex questions are always arose. Nevertheless it is hard to find a sufficient information regarding dealing with internal controls from the entity side in any scientific papers, therefore a structuring of information regarding test of controls by internal force has of very high importance.

Research. Internal financial control, as a part of financial controlling, is responsible for evaluation the effectiveness of internal controls at enterprise, which designed to prevent or detect risk of material misstatement (RoMM) or risk of fraud in company's financial statements. Internal controls may exist at various level of organization, and for better understanding of how internal controls were implemented and designed COSO framework is widely used. COSO framework provides a principled-based model to understand and think about internal controls in an organization [1].

According to International Standards on Auditing (*ISA 330 4.b*) **test of controls** is an audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level. Therefore, the purpose of the test of controls is to understand whether control is designed appropriately and operates correctly during tested period (usually one financial year).

There are four types of testing the controls at enterprise:

1. **Inquiry** usually means oral conversation with holder of control process or management regarding its design and effectiveness. According to *ISA 330 A26*, inquiry alone is not sufficient to test the operating effectiveness of controls.

2. **Observation** is looking at somebody, who is performing control procedure at specific point of time. Observation can provide assurance at the specific

point of time, therefore it is useful for obtaining evidence regarding control existence and does not give assurance over the control process quality. An example of observation of control could be inventory stock-take or PPE physical observation.

3. **Inspection** is often related to manual controls in a form of document examination (paper or e-documents). Inspection is an observation of control results. Example of inspection could be CFO monthly approval of discounts to main customers in a form of e-mail. Therefore, testing unit will be e-mail from CFO. Absence of e-mail could indicate that control is not appropriately executed and further procedures will be necessary to indicate effectiveness of control and deficiency at design or operational level.

4. **Reperformance** means independent execution of control by financial controller. Example of reperformance could be reconciliation of cash balance per general ledger to client-bank. This type of testing gives the highest level of assurance; however, financial controller should assess efficiency of following test as its time consuming.

Conclusions. The most effective type of test of internal controls is reperformance, at the same time it is the most time-consuming method, therefore financial controller before testing of controls should assess timing and extent of a test along with expected level of assurance to be obtained from it. The relationship between level of assurance and type of test of control is presented in *Figure 1*. However, a financial controller may also use several types of test of controls in order to receive desired level of assurance over control design and effectiveness.

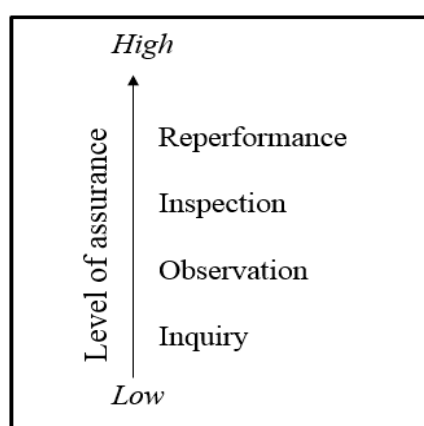


Figure 1. The linkage between level of assurance and type of test of control

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Capital Investment Decisions

Motivation. Of all the decisions that business executives must make, none is more challenging — and none has received more attention —than choosing among alternative capital investment opportunities. What makes this kind of decisions odemanding, of course, is not the problem of projecting return on investment under any given set of assumptions. The difficulty is in the assumptions and in the irimpact