

# Auditing - understanding and assessing internal control

[Finance](#)



## Homepro - Auditing - Assessing Internal Control Homepro - Auditing - Assessing Internal Control

Risk of material misstatement

Level of risk

Heads affected

1. As this is first year of audit, there is an inherent risk that the predecessor auditor has not properly examined the account balances in the financial statements and there are some uncorrected errors affecting the current year's audit opinion (AUASB, 2009).

Financial statement risk

Not applicable

2. The internal audit should ideally be reporting to the audit committee or chairman of the company (Grant Gay, 2012). In this case internal audit reports to CFO, which creates independence threat, and CFO may not intimate the weaknesses in the internal control system, which may result in material misstatement.

Financial statement risk

Not applicable

3. There is a risk of window dressing from store managers in order to achieve higher bonuses. They may use techniques to alter the figures of the inventory as to avail the bonus for example by not recording the last day inventory as to show a better inventory management which will ultimately result in understatement of inventory and payable balances.

Financial Statement risk

Inventory

Creditors

Cost of sales

4. The risk in this case is that, the remaining staff may not possess the same level of skills. They may be unable provide with the quality of service required to detect, prevent and correct the misstatements. Fewer numbers of people in the internal audit department will also put extra burden of responsibility on the remaining staff so, the level of care could also be compromised resulting in non-detection of misstatements.

Financial statement risk

Not applicable

5. The risk in this case is that the quarterly financial statements are not presented to the bank as required and it withdraws the credit facility. If this happens, there is a danger that the Homepro would have liquidity problems, which may prevent the company to carry business and revenue is lost. There are also chances of window dressing.

Assertion level risk

Revenue

Receivables

Cost of sales

6. Increased use of online shopping is a threat to the Homepro, since it may have serious effects on revenue (AUASB, 2009). There is a possibility that the opening of the online store would be delayed and the revenue would be lost. There is a threat of revenue being overstated to present a better picture for example, by recording revenue receipts, which pertain to next year.

Assertion level risk

Revenue

Receivables

Cost of sales

Inventory

7. The increased competition would force price cuts, which would ultimately result in decreased revenue and decreased profits. There are chances of revenue being overstated, or non-recording or delay in recording of expenses to show better profit figure for example by not recording year end expenses to show lower cost of sales.

Assertion level risk

Revenue

Receivables

Inventory

Payables

Cost of sales

8. Although the staff has been trained properly to handle the changes in the information system due to up gradation but still there are chances of mistakes in data recording so, there may be errors in recording of data which may either individually or collectively lead to material misstatement.

Financial Statement risk

Not applicable

9. In this case, the risk is the non-compliance with accounting standard. For example, provision regarding the share option is not made at fair value when it meets the recognition criteria as per IAS 1.

Assertion level risk

Provision

Equity

10. Resignation of the CFO may have severe effects on financial matters. In the absence of CFO there is a serious danger of non compliance of corporate governance and accounting standards . However, there is also a possibility that he was forced to window dress the accounts or to hide a major misstatement or fraud.

Financial statement risk

Not applicable

List of References

AUASB, 2009. Initial Audit Engagements—Opening Balances, ASA 510.

Melbourne: Auditing and Assurance Standards Board (AUASB).

AUASB, 2009. Identifying and Assessing the Risks of Material Misstatement through Understanding the environment, ASA 315. Melbourne Victoria: Auditing and Assurance Standards Board.

Grant Gay, S. R., 2012. Auditing & Assurance Services in Australia. 5th ed. North Ryde, N. S. W: McGraw-Hill Education.