

Internal Auditing

Student: Maria Falquet Torres (email: al258237@uji.es)

Tutor: Idoya Ferrero Ferrero

Finance and Accounting Degree

Year 2017/2018



ABSTRACT

In the last years, internal auditing has significantly evolved and has been established as a main tool for the enterprises' operating framework due to its economic complexity, the uncertain context where risk management is important, the introduction of new technologies and their excessive growth.

In this study we have briefly analysed the conceptual framework of the internal audit, revising the main concepts and relating them to other relevant concepts. Finally we have carried out a real practical case of a multinational group that is in full growth and belongs to the aquiculture sector.

TABLE OF CONTENTS

1-INTRODUCTION	4
2-CONCEPTUAL FRAMEWORK.....	5
3. DEVELOPMENT OF THE CASE STUDY.....	15
3.1 PLANNING	16
3.1.1-QUESTIONNAIRE OF INTERNAL CONTROL ENVIRONMENT	18
3.1.2-RISK MANAGEMENT MATURITY QUESTIONNAIRE	19
3.2 EXECUTION	21
3.2.1 RISK IDENTIFICATION	22
3.2.2 ANALYSIS AND RISK ASSESSMENT	25
3.2.3 DEVELOPMENT STRATEGIES.....	29
3.3. COMMUNICATION OF THE RESULTS	33
3.4. MONITORING	33
4-CONCLUSION AND RECOMMENDATIONS.....	34
5-REFERENCES	36
6-ANNEXES	38

INDEX OF FIGURES AND TABLES

FIGURE 1. COSO FRAMEWORK.....	9
FIGURE 2. ORGANIZATIONAL STRUCTURE	16
FIGURE 3. RESULTS OF THE QUESTIONNAIRE	19
FIGURE 4. RISK MATRIX OF THE COMPANY.....	29
FIGURE 5. RISK MATRIX OF THE COMPANY AFTER THE IMPLEMENTATION OF STRATEGIES	32
TABLE 1.CORPORATIVE VALUES.....	17
TABLE 2.RANKING CRITERIA	25
TABLE 3. RISK IDENTIFIED.....	27
TABLE 4. RISK IDENTIFIED.....	30

1. INTRODUCTION

According to Arens (2007), an internal audit is “an independent objective consulting activity designed to add value and to enhance the operations of an organisation. It helps the organisation to achieve its goals by providing a systematic and disciplined approach which will allow us to evaluate and to improve the effectiveness of risk administration, control and management processes”.

The term of internal audit is not a new concept; it dates back to the 1920's when big companies endorsed the idea that audits of financial states were not enough. From then on, the role of internal auditors involved having a detailed analysis of the internal control and of the company's information, which was not taken into account by the external audits.

Different concepts of internal audit will be explained and clarified in this thesis. We will see what an internal audit is, what are its elements just like a deeper analysis both theoretical and practical about what an internal audit is based on the risks.

A connection point between all the definitions found for internal audit is the evaluation of internal control; which plays a key role in the objectives of this work, being one of its main objectives relating the internal audit, the internal control and the risk management. In order to be able to relate all them, we will use the COSO models, the model based on ERM and the audit based on the risks.

This thesis includes different parts. First of all, we will find the theoretical framework, which includes different perspectives about the internal audit, the internal control and the audit based on risks. Secondly, we will see a case study on the basis of the risk-based audit in which the part developed in the previous conceptual framework is put into practice.

The main objective of this thesis is the theoretical and practical analysis of the internal audit just like paying attention to its results in order to verify that the internal audit has a key role in the management of companies.

The analysis of the study case is based on a real company. It is a multinational group from the aquaculture sector, which for several reasons and in order to preserve its anonymity we will call, from now on, Company A.

This thesis details the development of a risk-based audit model. The main objective of the study case of Company A is to do an evaluation of the company's risks approach for the goods purchasing process so we can provide them a business consultancy, assurance and maintenance service for an effective control system in the company. To do so, after the development of the study case and as the last part of the thesis, we will carry out several detailed conclusions and recommendations so they can represent an improvement for the company.

This thesis is divided in four points. We have already seen the first one in which we have introduced the work. After this introduction we will find the theoretical framework which puts us within the internal audit and ready to tackle the next point that is the practical analysis of the internal audit where all the risks that the company should face during the process analysed, the purchasing process, are explained.

2. CONCEPTUAL FRAMEWORK

The term audit is originated from the necessity to verify in order to reduce mistakes, both internally and externally. Accounting historian Richard Brown specifies that "the origin of auditing goes back to times scarcely less remote than that of accounting. Whenever the advance of civilization brought about the necessity of one man being intrusted to some extent with the property of another, the advisability of some kind of check upon the fidelity of the former would become apparent" (cited in Mautz & Sharaf, 1961).

According to the American Association (AAA, 1973) auditing is "a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria, and communicating the results to interested users."

Among the most common classifications we can distinguish different types of audits depending on its purpose and criteria. On the one hand, the analysis is based on who audits, in other words, according to the origin of the auditing team; and it is distinguished between internal audit and external audit. On the other hand, we can outline three types of audits based on their purpose: compliance audit, performance audit, and financial statements audit. Even though they are not the same terms, there is a great similarity between internal audit and performance audit, and external audit and financial statements audit.

External audit is in charge of examining the financial statements of a company by a qualified and independent expert. This is done with the objective of expressing the expert's opinion about the financial statements and according to certain procedures and rules.

External audit is defined as “a periodic examination of the books of account and records of an entity carried out by an independent third party (the auditor), to ensure that they have been properly maintained, are accurate and comply with established concepts, principles, accounting standards, legal requirements and give a true and fair view of the financial state of the entity” (Chartered Institute of Management Accountants, 2005).

Internal audit is a type of audit carried out by the organization to assess its performance. It is carried out as a consequence of an internal requirement of the very own company. Internal auditing consists in assessing the different procedures adapted by the company and its internal control to be able to know if the functioning that they have is the one established. If that is not the case, it is used to suggest changes and improvements in the processes to achieve an effective internal control. In June 1999, the Institute of internal auditors approved a new definition of the internal auditing function. And it defines that the internal audit is “an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes” (IIA, 1990).

Another definition of internal audit according to the International Standards on Auditing (ISAs) is the following: “assessment activity established or borrowed to the organization as a service. Its functions include the examination, evaluation and monitoring of the internal control adaptation and efficacy” (NIA, 2013).

There are many definitions of internal audit; despite being very similar, each author or institution refers to different things. The linking point between all of them is the internal control assessment, or in other words, the internal control system that companies use. The evaluation of the internal control system carried out by the internal auditor is used to solve problems that the company might have, assess how the different procedures are working in order to make a diagnosis and decide the organization's strengths and weaknesses.

Internal control is not a new term; it exists ever since the first organizations were created because of the necessity to establish control over the operations and people who participate in them. It is a key element in the performance of the companies and it has a big impact on the quality and veracity of the produced information.

According to the *Spanish Technical Standards on Auditing (Normas Técnicas de Auditoría)* issued in 1991 by the Institute of Accounting and Accounts Auditing (*Instituto de Contabilidad y Auditoría de Cuentas*) or ICAC, internal control is defined as “a process designed, implemented and supported by the governants of the entity, its Executive Management, and other members of the staff, in order to provide a reasonable security about the objectives’ achievement of the company that are related to the liability of the financial information, efficacy and efficiency of the operations, as well as the compliance of the legal and regulatory applicable requirements”.

As mentioned above, there are different definitions of internal control and its related terminology. Due to this fact and in order to collect all the conceptual terminology, the Treadway Commission prepared a report to be able to create a common concept useful as a reference point. The Committee of Sponsoring Organizations of the Treadway Commission (COSO) was created and it conducted a study in relation to the development of frameworks and orientations that covers internal control and risks management.

According to the COSO report (1992) the definition of internal control is: “a process, effected by an entity’s board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting, and compliance.”

The COSO report establishes different categories of objectives that allow the organizations to be able to focus on different aspects of internal control.

- Operations Objectives: related to the efficiency and effectiveness of the operations carried out by the entity.
- Reporting Objectives: referred to the financial and non-financial reports, both internal and external that can comprehend liability, transparency and opportunity.
- Compliance Objectives: those referred to the regulations that the entity is subjected to.

The COSO model (1992) establishes that internal control is formed by five integrated components that have to be executed by the company in order to make internal control efficient. The COSO model framework was updated in 2013. Each company will establish the components according its type of management and philosophy. The integrated components appear in figure 1.

FIGURE 1. COSO FRAMEWORK



Source: COSO REPORT (1992)

In order to make internal control effective, five components must be accomplished. This does not mean that all components have to work in the same way, but they have to always work with the purpose of protecting and supporting the achievement of the company's objectives and strategies.

- Control Environment

Control environment is each aspect that has an influence in the activities carried out by the company. It is considered a key element in any system because it determines the company's organization pattern and it influences the attitude that the staff has towards control.

- Risk Assessment

It is the analysis of the risks that could affect the entity and it establishes different strategies to face them. In order to accomplish this analysis, the organization has to lay

down its objectives, and it has to inspect each risk for each objective. Once the risks are identified, they have to be analysed and classified. Finally, after the analysis of the risks, the decision about how to manage them will be made.

- Control Activities

They are carried out by the management and staff in order to fulfil the assigned tasks that appear in the organization policies and procedures. The control activities and tasks are addressed towards risks, having the organization's benefit always in mind and that is why they are so important, because they assure the achievement of the company's objectives.

- Information and Communication

Information and communication are key elements in the operating of the other control components. On the one hand, when we talk about information we are not only referring to a combination of data but to a combination of data ready to be analysed and presented adequately. Currently there are many powerful programs and applications to manage information that used properly can be a very effective control component. On the other hand, information must possess proper communication channels so all organization components are aware of their responsibilities towards control.

- Monitoring Activities

Monitoring activities are procedures to assess if each of the control components works properly. According to COSO, monitoring activities can be executed in two different ways. On the one hand, ongoing evaluations are those that are carried out like a routine job as a part of the process that is undergoing assessment by the staff of the entity. On the other hand, separate evaluations are those carried out by external staff like internal or external auditors; these evaluations don't happen constantly but at a specific time.

As a response to a series of irregularities and the possibility of error and frauds appearance inside the companies' organizations due to a change in the business environment, the Treadway Commission developed the Enterprise Risk Management (ERM) in 2004 in which the concept of internal control was expanded. It is worth mentioning that the new approach does not replace the previous conceptual

framework, in fact it assimilates it providing a larger and more concrete approach about risk identification, assessment, and management.

Enterprise Risk Management (ERM) is a process that allows the efficient identification of uncertainty through risk and opportunities identification optimizing value creation. This process contributes to obtaining solutions in opposition to the identified risks and allows better practices to be applied.

ERM points to risks and opportunities that affect the company's value. It is a process done to identify the events that can damage an entity and manage the risk so it is inside the risk appetite in order to facilitate a reasonable security to the company's objectives consecution (COSO 2004).

According to Institute of Chartered Accountants of India (2007) Enterprise Risk Management is defined "as a process, affected by an entity's board of directors, management, and other personal, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives."

The term "risk appetite" mentioned above refers to the risk level that the Board is willing to accept to meet the objectives; it provides a guideline to be able to start comparing a risk. If the risk is above the risk appetite it will be considered a threat to the achievement of the objective.

According to the framework clearly defined in the COSO report, ERM lists eight components to control risks. These are originated from the way in which the administration manages a company and the way they are integrated in the management process. These components are:

- Internal environment: it covers the environment in which an organization works and establishes the basis for risk to be seen and tackled.
- Objective setting: the objectives must be known and established, at the same time they have to support and be in accordance with the entity's mission.
- Event identification: the internal and external events that affect the objectives achievement of the entity must be known, and we have to clearly distinguish between risks and opportunities.
- Risk assessment: risks are assessed considering both their probability and their impact, and are evaluated from a double perspective: inherent and residual.

- Control activities: they are established and they apply procedures to ensure that risk responses are carried out in the best possible way.
- Risk response: the administration fixates and selects risk responses to be able to accept, reduce, or prevent risks by placing them with the risk and the company's risk tolerance.
- Information and communication: relevant information is identified and notified to the people in charge of the company so they can perform their responsibilities.
- Monitoring: the whole risk management is supervised through management activities and evaluations.

ERM is a new approach in which business risk is evaluated, managed, and notified. Therefore, it contributes importantly to companies to manage their risks to be able to face their objectives' achievement.

Internal auditors play a key role in evaluating risk management due to the fact that internal audit is in charge of evaluating the risk management process with the goal of providing certain trust to the company; planning resources and achieving all the possible objectives will reach an effective internal control.

Risk-based auditing is one that verifies that the audited processes meet the objectives of the company in an efficient and effective manner. First, it evaluates the effectiveness of internal control; determining the ability of controls to reduce levels of potential risks. And secondly, it checks that the controls for the risks that weaken the control are fulfilled.

Risk-based auditing is one that evaluates and checks that the audited processes meet the objectives of the company in an efficient and effective manner. First, it evaluates the effectiveness of internal control; determining the ability of controls to reduce levels of potential risks. And secondly it checks that the controls are fulfilled for those risks that show weaknesses in the control.

Referring to (Koutoupis 2005) "Risk assessment consists of risk identification and risk analysis. Risk identification includes examining external factors such as technological developments, competition, economic changes, etc. and internal factors such as personnel quality, entity's nature of activities, the characteristics of information system processing, etc. Risk analysis involves estimating the significance of risk, assessing the likelihood and impact of the risk occurring, and considering how to manage risk."

The main objective of the audit based in risk is being able to distinguish the most relevant risks from the less relevant in order to tackle them effectively.

According to the internal audit guide based on risk of the Institute of Chartered Accountants of India (2007), there are five risk maturity levels:

- Risk Naïve

The company has not developed any determined approach for risk management.

- Risk Aware

The company has identified risk inside the company's roles but not in the processes. Moreover, risks have not been notified by the company.

- Risk Defined

The company has defined the risk appetite, and established and notified its strategies and policies.

- Risk Managed

The company has a developed approach for risk management and it is notified.

- Risk Enabled

Next, we will explain the different risk levels that have been established through internal control, and risks will be examined considering both the risk consequence and their likelihood of occurrence, therefore the risk evaluation that the company is exposed to will be obtained.

Another key aspect for risk analysis is establishing different risk levels. Next we will explain the different risk levels that have been established through internal control (Institute of Chartered Accountants of India, 2007).

- Inherent risk: is the risk that is subjected to an activity or process before an internal control technique is applied.
- Residual risk: is the tacit risk in the activities or processes after the company has taken the internal control actions.
- Risk appetite: is the number of risks that the company is willing to accept to reach its goals and objectives. If the risk is below this limit, it means that it is on the desired level.

- Risk tolerance: is the quantity of insecurities that a company is willing and ready to accept, or the maximum risk quantity that is ready to accept to reach its objectives. Risk tolerance is normally notified in terms of acceptable or unacceptable; risks that are above this risk level are considered unacceptable.
- Risk capacity: is the maximum risk quantity that an organization can accept in order to reach its goals and objectives.

Right after, risks are explored considering both the risk consequence as well as its likelihood of occurrence, therefore they obtain the risk evaluation that the entity is exposed to. In order for the company to take action facing the different risks, it is necessary to establish an assessment to resolve the company's most critical risks.

Once the entity's exposure to risk has been obtained, this will be measured through a tool called risk matrix. Risk matrix is a control and management tool to identify the type of risk and its level for each activity or process of the company.

Once the most important risks have been detected and analysed (those that have the highest impact and likelihood of occurrence due to the fact that if they happen they can have a big effect for the company), the strategies' development is executed to manage and reduce risk.

Once the threats have been identified, the most important aspect of risk analysis is identifying controls to reduce both their impact and likelihood of occurrence.

There must be an individual decision for each of the risks. The company can face the risk in four different ways: tolerate it, mitigate it, transfer it, or erase it.

- Erasing the risk; it means that activities that cause this risk are abandoned.
- Sharing and transferring the risk; transferring its impact to another project's external element, therefore the risk will have been erased. We have to take into account that we have to know the capacity that it has of accepting the risk of the external element we are transferring it to.
- Mitigating the risk through the company's strategies and tools.
- Tolerating the risk; no measures will be taken against them, therefore risk is avoided as if it wouldn't exist.

Finally, the auditor will create the risk matrix after the development strategies and will notify his or her recommendations. The last step will be supervising that the company carries out the recommendations to reach an effective internal control.

3. DEVELOPMENT OF THE CASE STUDY

The study will focus in the practical case of a company that belongs to the aquatic sector; with educational purposes and in order to keep its anonymity, the company will be called A. Through the following fragments, we will assess the operating way that the company's sectors have, or in other words, how the different management areas of the company work.

This internal audit will try to assess and identify the risks that are not being taken into account by the company, applying certain procedures that will allow the verification and assessment of the work done. According to Hevia (1989) "risk identification is the creation of a risk inventory that threatens the company calculating its potential consequences".

We will assess the risk evaluation using the approach mentioned in the conceptual framework, the internal control COSO approach and referring to the *Manual práctico de control interno de Barquero (2012)*. Then we will carry out the practical case of the four stages of internal audit of the Company A.

According to the Institute of Chartered Accountants of India (2007), the internal audit process has the following stages:

- I. Planning
- II. Execution
- III. Report submission
- IV. Supervision

The study is based in a multinational group that develops its activities in the aquaculture sector; this company is Company A.

Company A is the fastest growing group of companies in the Mediterranean Aquaculture industry, with activity across Europe and with worldwide export power as well.

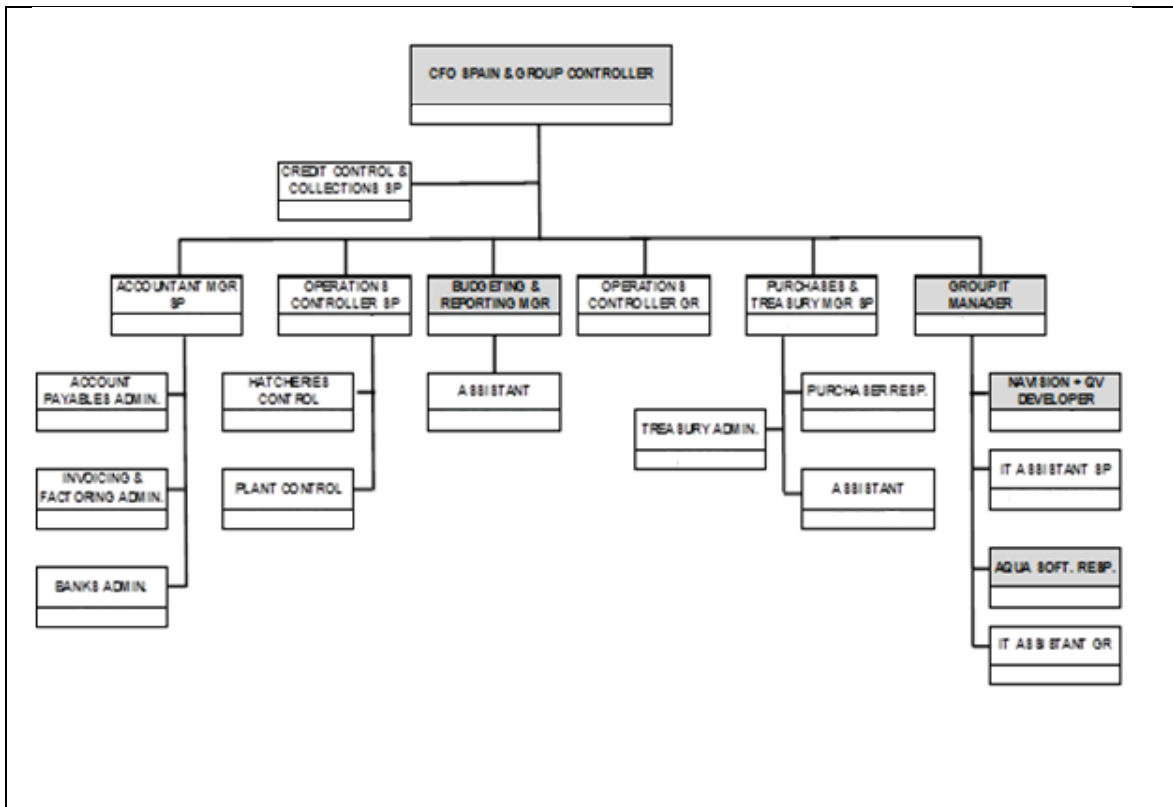
The main attribute of this company is the high quality and true freshness of its products; combined with a sophisticated distribution network that facilitates delivery of its products throughout Europe within only 48 hours from harvesting.

3.1. PLANNING

In this first stage of internal audit, the company provides the auditor with the necessary information to have the company's context knowing its functioning and processes to be able to define successfully the established objectives.

Due to the big size of the company and in order to simplify the task, this study will focus on the subsidiary group in Spain. This company has a defined mission, vision, organisational structure, and internal control adapted to the company's characteristics. The organisational structure of the group's administration is shown in figure 2.

FIGURE 2. ORGANIZATIONAL STRUCTURE



Source: Proper making

Table 1 shows the frame of reference and different established values that the company uses for its employees.

TABLE 1.CORPORATIVE VALUES

MISION

To create quality and high-value added products through a productively innovative and excellent task based on deep knowledge of the marine ecosystems; as well as actively contributing to the protection of the environment.

VISION

To be a leading company in the fishing and aquaculture industry being sustainable in the use of the resources, taking care of the environment and creating value for its stockholders, customers, and employees, as well as delivering products and services with highly regarded standards in the markets we are present at.

STRATEGICAL OBJECTIVES

- Keep the quality and improve the processes.
- Expand our products all over the world.
- Constant learning and appliance of the highest quality standards.
- Combine the principles of excellence, responsibility, loyalty, and commitment to people and the environment.

Source: Proper making based on Web Company.

Nowadays, the group has two bases in Greece and Spain with similar volumes. The headquarters is in Spain although the executive team is in Greece. In Spain, the company has 250 employees and a volume of business of 63,190,199 euros. Once we have mentioned the basic aspects of the company, we will write about the economic profitability or the return on assets (ROA) which is of 7.11% in 2015. Another worth mentioning ratio is the return on equity (ROE) of 2015 which was of 16.53%.

3.1.1.QUESTIONNAIRE OF INTERNAL CONTROL ENVIRONMENT

Control environment is key for the design of internal control in which we can see the importance that the company's management gives to internal control and how this translates into the activities and results of the company. According to Rio Del Toro et al (2005), for the development and evaluation of this mechanism there are seven key components:

- Integrity and ethical values
- Professional expertise
- Control committee
- Mutual trust environment
- Organisational structure
- Assignment of authority and responsibility
- Policies and practices related to the staff

Control environment is essential for any control system. To understand the organization's environment better, as a preliminary evaluation of internal control, a questionnaire will be carried out with a group of questions oriented to check the company's internal control. Questions are formulated so an affirmative answer denotes strong internal control and negative answers denote weakness.

To be able to receive the required information for the case study, these questionnaires and meetings have been done by the staff that is in charge of the main areas of the company, and will be responsible of answering the questionnaires ready for preliminary evaluation.

The control environment questionnaire used for the evaluation that is attached has the same questions that appeared in Rio Del Toro et al (2005) work about Internal Audit.

FIGURE 3. RESULTS OF THE QUESTIONNAIRE



Source: Proper making

Figure 3 shows the results of the questionnaire, where it is observed that Company A has a balanced control environment. Annex 1 shows the questionnaire on the internal control environment that has been made to the controller of the company.

3.1.2.RISK MANAGEMENT MATURITY QUESTIONNAIRE

The risk management maturity questionnaire is answered by the company's manager and it refers to the maturity level of the control system established by the company. It is important to know the maturity level because it will allow us to know if the company has restraints when having a desired internal control system and if it has an incorporated management system. Considering that if it does not, most of the monitoring is done manually and has greater chance of error. The importance of risk maturity is because the audit is strategy depends on it (Institute of Chartered Accountants of India, 2007).

Therefore, the approach to internal audit is determined by the risk maturity level; to evaluate it in this practical case we have done a risk maturity questionnaire that you can find in the Annex 2.

After the realization of this questionnaire, the following was concluded:

On the one hand, there is a high management maturity level considering that risk management is developed and informed constantly according to the company's value chain precedence. On the other hand, there is a deficiency because the risk appetite has not been defined by a rating system.

Regarding the questionnaire rating, it has been risk defined, meaning the company has a high level of understanding about risk management.

The main objective of internal audit in Company A is the realization of an evaluation of the risk management processes in order to provide security to the company maintaining an effective internal control.

During the planning stage, all the different aspects to know the significance of auditing must be determined.

- Auditing team

The auditing team is in charge of internal audit. They can be related to the company as long as they can be impartial during the process. These people will not be in the audited department because it is unviable to audit your own work.

- Duration of internal audit

The audit is duration was established to be of two and a half months due to the characteristics of the company and the selected process. Therefore, internal audit began in March and ended in late May with the results' presentation. In the Annex 5, you can find the work table done for this audit.

- Field application

The audit for development is applied to the company's administration department because they do a big number of procedures and processes. Inside the administration department there are a lot of processes and that is why the internal audit will focus on a specific process: purchase of goods.

According to Baquero (2013) a purchase process can be divided in the following subprocesses. These next subprocesses (that we will explain next) will be analysed in the group's internal audit.

- Provider selection

The purchase of goods process begins selecting the providers we are going to work with. For this reason, the purchase department is in charge of negotiating the economic conditions with the providers according to the technical requirements. Once the providers have been chosen, the department proposes the one who offers better economic terms and from now on the staff responsible of the process will be who will pick the best option and authorize them to introduce them into the providers' data base.

- Placing orders

Based on the necessities requested by the different company's areas, the purchase department sends the orders to the authorized providers. The orders, depending on their cost, will need to be authorized or not.

- Goods receipt

Goods are received in the warehouse and are registered in the inventory, checking the merchandise with the received dispatch note. The entrance in the inventory is taken into account as an increase in the stock and as a provider's debt because of invoices pending receipt. Its manual or automatically accounting can begin.

- Invoice receipt

Afterwards, the provider sends the invoice and the department checks if the invoice is correct according to the received goods through the dispatch note. If it is correct, it is accounted reducing the balance of invoices pending receipt.

- Invoice payment.

Based on already accounted invoices, every month the liquid assets department prepares the relation of the accounted invoices and proposes the payment authorization to the staff with banking power. If this payment is authorized then it starts and it is accounted in the provider's account.

3.2. EXECUTION

Once the previous phase has been explained, we proceed to the execution of the auditor's work in which we will identify the events. This following phase will be divided into different parts.

3.2.1. RISK IDENTIFICATION

In order to have a good understanding of the risks identification, we should first know the concept of risk. Risk is the possibility that an action may affect in some way an entity, Chambers (1992).

Hevia (1989) defines the concept of risk from a more economical perspective, as “something that if materialised can produce both, positive effects for the company (strengths and opportunities), and negative effects (weaknesses and threats)”.

There are several classifications for risks from the company’s administrative view. Rio Del Toro et al, (2005) have classified financial risks in speculative and pure risk, being pure risk classified as inherent and embedded.

- External risk, which is the one that may produce losses and profits and that does not depend on the company’s administration itself, but on the exterior.
- Internal risk, which is the one that takes place in the company itself and that it is associated with the company’s activities. Within this, we can distinguish between inherent risk, which is the one that it is typical of each company and that comes from the business activity’s nature making them the risks that the company should accept, control and eliminate. We also have the integrated risk, considered as a second level risk because of it being a product of the behaviour carried out by the company’s staff; this type of risk should be eliminated immediately.

Risk identification is a process that recognises what can occur and why it can occur in the execution of the tasks needed to carry out an action. According to Koutoupis (2005), the identification of risks consists of examining the nature of the activities, the external and internal factors, the characteristics of the information systems and the processes in which the entity operates.

According to Arce (2005), “The identification of the risks is one of the most important elements, in our opinion, to foster the entity to achieve administrating the risks successfully and to know the different elements which in some way will have influence the exposure of the company to uncertainty”.

The auditor of Company A considers that the operational risks in the purchasing department may be associated to the people, the technology and the processes involved in the execution of the activities.

For the compilation of relevant information for risks identification, different tools and skills are used. Some of these tools are questionnaires, flowcharts, interviews, observation and inspection and participation in meetings (Carias Santos, Martinez Estrada, Diaz, 2011). In the internal audit of the goods purchasing process in Company A, the techniques used are interviews, questionnaires and flowcharts.

- **Flow chart**

A flowchart is the graphic representation that itemises an administrative process. It is a very important instrument because of its help by using a graphic representation in order to understand the process, the methods and its operation well with the purpose of enhancing them and increasing the existence of information systems. It allows you to have a better display of the activities and a better work distribution.

If the audited entity has defined a system of control and its appropriate diagrams in purchasing department, the internal auditor must check that the flowchart is updated and that it reflects the reality of the process. Otherwise, the auditor should develop the flowchart by himself/herself.

In the case of Company A, the company hasn't any organisation chart of the process, so it is been carried out by the auditor according to the information given by the purchasing department of the company. The organisation chart (made by the auditor), which is very useful to detect events, is in the appendix section and it shows clearly the process of purchasing goods.

Appendix 3 shows the flowchart for the purchasing goods process.

- **Questionnaire for the purchasing process**

The questionnaire technique about the audited process is very useful to analyse a specific department in the company because it clarifies all the doubts related to the way of doing operations and to the processes used.

The questions from the questionnaire of the purchasing department have been asked in order to have two possible answers, one affirmative and another one negative, so in this way it is possible to identify the negative events of the process. The main purpose for its wording is to make its response easier for the staff and to carry out its analysis.

For the elaboration of the questionnaire, several models of draft questionnaires have been used, of which a series of questions have been selected to develop our own questionnaire.

The person responsible for the purchasing process answered the questionnaire, so the questions with a negative response were a sign of something that could lead to a risk.

Appendix 4 shows the questionnaire.

After completing the questionnaire and making a flowchart of the purchasing process, the results were analysed and it was possible to identify the events in the process as they can influence to achieve the aims. The events found are the following:

- 1.The selection of the best option of the offers obtained by the purchasing department is not taken jointly between the responsible of purchases and the one of production.
- 2.Not only the authorized person in the purchasing department can enter suppliers in the system database, they can also enter it from the accounting department.
- 3.The average purchase price is not checked in each order made and for each product reference, comparing them with the budget, with the previous year and with the evolution of the cost of materials. .
- 4.It is not reviewed that the stock levels for each reference being purchased are reasonable to the needs.
- 5.Inventories made during the year, are not made by people outside the daily management of the warehouse.
- 6.The cost of purchases made is not automatically accounted for the amount resulting from the inputs quantities of product entries and prices of the order placed, with an account of invoices pending receipt.
- 7.Personnel who enter invoice data into the system do not associate it with an order (normally the supplier is required to refer to the order number on their invoice), but suppliers are not required to refer to Order on the invoice. So the system does not compare that the invoiced amounts match those received, likewise does not verify that the prices of the invoice are those authorized in the system or those included in the order.
- 8.There is no segregation of duties between the people responsible for the purchasing process and the treasury.
- 9.There is no correlation between physical and digital information.

3.2.2. ANALYSIS AND RISK ASSESSMENT

According to Barquero (2012), a part of the internal control is the fact that the management must analyse and document all the risks that may affect the entity. Once these risks have been identified, they must be analysed and classified according to variables such as:

- Probability of occurrence.
- Magnitude of the impact.
- The time.
- The persistence of the impact once the risk has occurred.

In order to simplify the elaboration of this practical case of the four variable used by Barquero, we are only going to take into account the magnitude of the impact and the probability of occurrence.

In order to estimate and measure the risk, 5 levels are listed depending on the severity of the impact and the probability of occurrence, for the later decision-making. In the risk matrix, both the assessment of the probability of occurrence and the assessment of the consequence of risk are represented; however other scales (classified in high / medium/ low types, as it is difficult to estimate in more detail) are also used, as Barquero (2012) explains in his manual.

In order to be able to establish this classification, the internal auditor should know the company really well and have some experience in the organisation.

Table 2 is shown below and presents individually the classification criteria for the risk variables according to the Institute of Chartered Accountants of India (2007)

TABLE 2.RANKING CRITERIA

VALUATION OF RISK CONSEQUENCE		VALUATION OF PROBABILITY OF OCCURRENCE	
DEFINITION OF THE IMPACT	DESCRIPTION OF THE CONSEQUENCE	PROBABILITY	DESCRIPTION
Catastrophic (5)	A catastrophic impact on the organization, it is	Almost certain (5)	Risk whose probability of occurrence is very high, ie,

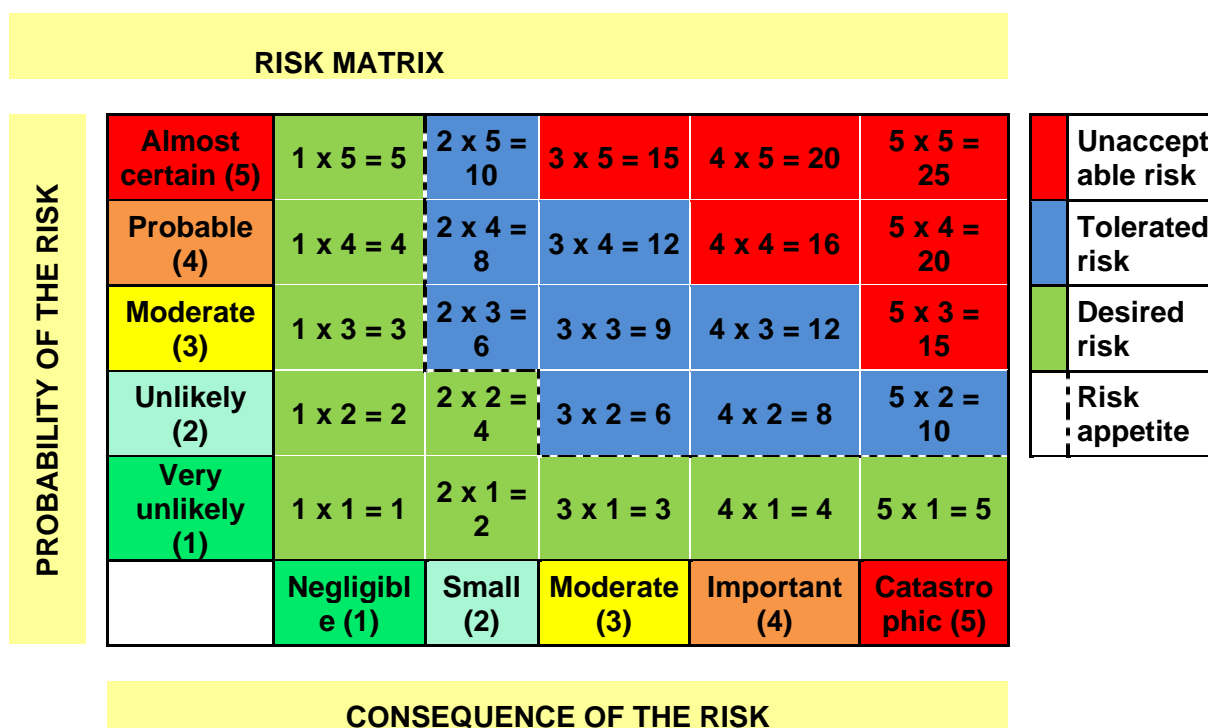
	doubted that it can face it.
Probable (4)	It does not allow the organization to achieve fully or in part the long-term objectives.
Moderate (3)	It does not allow the organization to meet its annual goals.
Small (2)	It does not allow the organization to achieve its quarterly objectives.
Negligible (1)	It does not affect the achievement of the objectives of the organization. It causes a minor inconvenience.

	it has a high degree of security that this present
Probable (4)	Risk whose probability of occurrence is high
Moderate (3)	Risk whose probability of occurrence is medium
Unlikely (2)	Risk whose probability of occurrence is low. It has occurred in the industria.
Very unlikely (1)	Risk whose probability of occurrence is very low. It has never happened in the industry.

Source: The Institute of Chartered Accountants of India (2007).

Once the exposure that the entity has on the risk has been obtained, we represent the risk matrix. In figure 4 it is possible to identify the matrix of risks with which Company A has established the different levels. It should be noted, as it was mentioned in the Risk maturity questionnaire, that the company has not the risk levels defined yet, so hypothetical levels have been established.

FIGURE 4 . RISK MATRIX



Source: Proper making

Once the questionnaires and interviews have been carried out and their risks identified, they are analysed and classified depending on the magnitude of their impact and their probability to occur. The table 3 that we are going to see next shows us the identified events and the risks, just like the impact and occurrence probability. Risk is quantified.

TABLE 3. RISK IDENTIFIED

Nº	Identification of the event	Identification of the risk		Evaluation of the Risk		
	Event	Classification	Risk	Probability	Impact	Inherent Risk
1	The selection of the best option of the offers obtained by the purchasing department is not taken jointly between the responsible of purchases and the one of production.	Internal	Association with suppliers in exchange for commissions to select their product	4	2	8
2	Not only the authorized person in the purchasing department can enter suppliers in the system database, they can also enter it from the accounting department.	Internal	Ordering from unauthorized suppliers	2	2	4

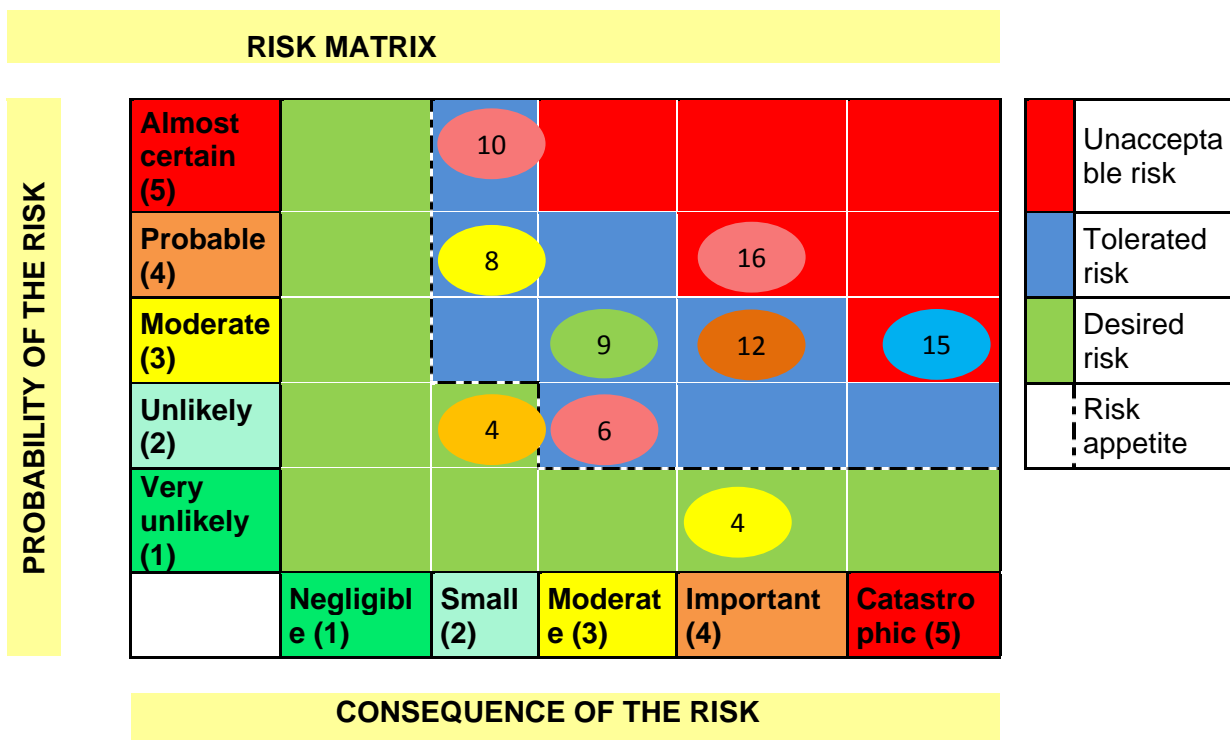
3	The average purchase price is not checked in each order made and for each product reference, comparing them with the budget, with the previous year and with the evolution of the cost of materials.	Internal	Orders at prices different from those agreed.	3	3	9
4	It is not reviewed that the stock levels for each reference being purchased are reasonable to the needs.	Internal	Unnecessary orders or fraud or error	5	2	10
5	Inventories made during the year, are not made by people outside the daily management of the warehouse.	Internal	Accept product quantities higher / lower than the orders for fraud or error.	1	4	4
6	The cost of purchases made is not automatically accounted for the amount resulting from the inputs quantities of product entries and prices of the order placed, with an account of invoices pending receipt.	Internal	Error in posting	4	4	16
7	Personnel who enter invoice data into the system do not associate it with an order (normally the supplier is required to refer to the order number on their invoice), but suppliers are not required to refer to Order on the invoice. So the system does not compare that the invoiced amounts match those received, likewise does not verify that the prices of the invoice are those authorized in the system or those included in the order.	Internal	Acceptance and posting of incorrect invoices for fraud or error	3	4	12
8	There is no segregation of duties between the people responsible for the purchasing process and the treasury.	Internal	Embezzlement	3	5	15
9	There is no correlation between physical and digital information.	Internal	Internal duplication or lack of information.	2	3	6

Previously we have been talking about the risk matrix and we have done the hypothesis of the risk levels because the company didn't have them defined.

In the following chart, figure 4, we can see the risk matrix with the risks from the previous chart identified and described which refer to the risks found in the purchasing department of Company A. As we can see, there are some risks which are acceptable, but most of the risks found are above the limit of risk desired (previously established by an hypothesis). We have only found one unacceptable risk, which needs a higher attention because of the high impact that can have for the company. It is important to say that the higher the risk, the more internal control must present.

Figure 5 shows us the risk matrix:

FIGURE 4. RISK MATRIX OF THE COMPANY



Source: Proper making

3.2.3. DEVELOPMENT STRATEGIES

Once the most important risks have been detected and analysed, which are those that present a higher impact and occurrence probability (since in case of occurring may have a big consequence for the company), we should develop strategies to manage and reduce the risk. As we discussed before in the theoretical framework, the decision can be eliminate, share or transfer, mitigate or tolerate the risk.

The following chart 4 refers to the development strategies carried out taking into account the risks identified for the company.

TABLE 4. RISK IDENTIFIED

Nº	Identification of the risk			Internal control		Evaluation of the risk		
	Event	Risk	Inherent Risk	Answer	Internal Control	Probability	Impact	Residual risk
1	1. The selection of the best option of the offers obtained by the purchasing department is not taken jointly between the responsible of purchases and the one of production.	Association with suppliers in exchange for commissions to select their product	8	Mitigate	Monthly take jointly the best offer.	3	2	6
2	1. Not only the authorized person in the purchasing department can enter suppliers in the system database, they can also enter it from the accounting department.	Ordering from unauthorized suppliers	4	Tolerated		2	2	4
3	The average purchase price is not checked in each order made and for each product reference, comparing them with the budget, with the previous year and with the evolution of the cost of materials.	Orders at prices different from those agreed.	9	Tolerated		3	3	9
4	It is not reviewed that the stock levels for each reference being purchased are reasonable to the needs.	Pedidos innecesarios or fraude o error	10	Mitigate	Review of stock levels for each product.	4	2	8
5	Inventories made during the year, are not made by people outside the daily management of the warehouse.	Accept product quantities higher / lower than the orders for fraud or error.	4	Tolerated		1	4	4

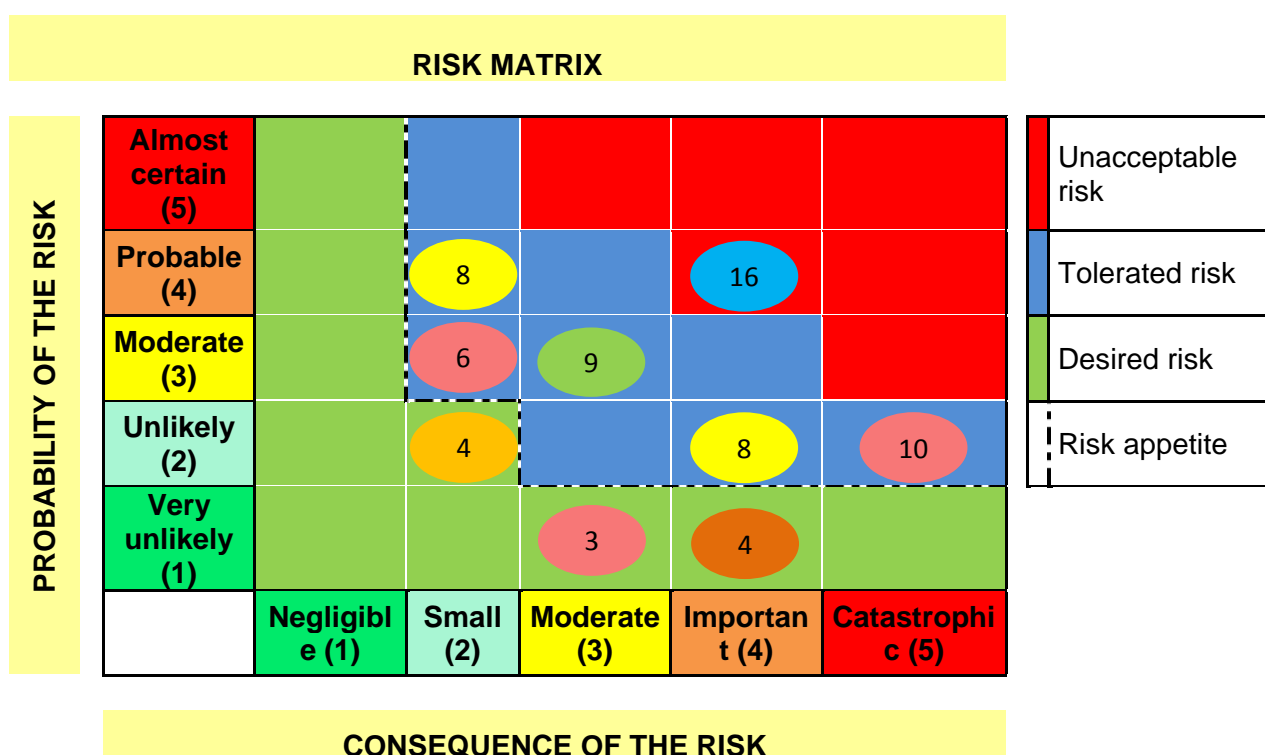
6	The cost of purchases made is not automatically accounted for the amount resulting from the inputs quantities of product entries and prices of the order placed, with an account of invoices pending receipt.	Error in posting	16	Tolerated		4	4	16
7	Personnel who enter invoice data into the system do not associate it with an order (normally the supplier is required to refer to the order number on their invoice), but suppliers are not required to refer to Order on the invoice. So the system does not compare that the invoiced amounts match those received, likewise does not verify that the prices of the invoice are those authorized in the system or those included in the order.	Acceptance and posting of incorrect invoices for fraud or error	12	Mitigate	Require the supplier to indicate the order number on the invoice	2	4	8
8	1. There is no segregation of duties between the people responsible for the purchasing process and the treasury.	Embezzlement	15	Mitigate	Technique Segregation of functions between people in the departments	2	5	10
9	1. There is no correlation between physical and digital information.	Internal duplication or lack of information	6	Mitigate	Monthly review of available information.	1	3	3

The main objective is to reduce the inherent risk, that's why some internal controls have been established. On one hand we have the response to the risk levels which are above the desired risk limit, which is the one that is not acceptable or even not affordable for the company and that is necessary to mitigate them. On the other hand,

we have other risks that have not been necessary or even possible because we are capable to tolerate and accept them. All this has happened because the costs to establish control techniques are excessive.

Figure 5 shows us the residual risks in the risk matrix after the implementation of several strategies by the internal control. It shows, in a graphic way, the effects that these control techniques have had in the detected risks, leading us to implement different strategies for the risks development.

FIGURE 5. RISK MATRIX OF THE COMPANY AFTER THE IMPLEMENTATION OF STRATEGIES



Source: Proper making

Once the control maturity has been determined, the auditor must give opinions and recommendations about the risks in which the controls, previously established by the company, are not sufficiently effective.

The main recommendations have been in the first place and looking in to the future, would be to implement a system of bar codes in which the amounts of product entries and the prices of said order to an account of invoices pending reception were recorded directly in the system. Another of the main recommendations is the preparation of a manual of procedures of the department so as to avoid many doubts and errors. And

the last and most important is the segregation of functions between the responsible for purchasing and treasury.

In Appendix 6 we can find a chart where all the recommendations for the risks made by the auditor in order to enhance the internal control system appear.

3.3. COMMUNICATION OF THE RESULTS

In this phase, close to the end of the whole process, the auditor must inform about the results of his/her work as well as the conclusions and recommendations drawn.

In Appendix 7 we can see the audit report carried out by the internal auditor.

3.4. MONITORING

In this phase, the auditor must inform about the corrective actions which should be applied taking into account the recommendations made in the previous phase.

It should be also ensured that the company is fulfilling the corrective actions. This phase of the audit is beyond the scope of this thesis due to time and complexity reasons.

4-CONCLUSION AND RECOMMENDATIONS

The main objective of this thesis has been to do a conceptual approach of the internal audit, taking into account that this process is gaining more importance or becoming more popular for big companies over the years.

First of all, we have presented a theoretical framework about the internal audit, we have seen the principal types of audits and we have explained the differences between internal and external audit. We have also developed the COSO model (1992) and its later revisions COSO (2013), which has been a very important reference for the development of this thesis. We have also contextualised the risk management model.

Secondly, once the conceptual framework for the Internal Audit has been clarified, we have started with the execution of its the study case. To do so the manual of Barquero (2012) has been crucial since in two of his chapters he refers to the internal audit in the goods purchasing process.

The study case, carried out for an aquaculture company, has tackled the internal audit of the purchasing process and has been done following step by step all what has been explained in the conceptual framework, getting to identify nine events. Once the events have been found and the internal auditor has already analysed and classified them according to their magnitude of impact and their probability of occurrence, the development of strategies to manage and reduce the risk has been executed.

After the analysis have been done, we have been able to provide several recommendations in order to mitigate the possible risks. These advice proposed by the auditor can be really important so the company could face the risks. Something that we should highlight of this part is the fact that the company should carry out a goods purchasing proceedings manual because it'd eliminate the errors and doubts by the existent staff and it'd make the learning and comprehension process easier in case of the arrival of new employees to the area.

As possible future phases, we could highlight the monitoring activity; which is following up the recommendations exposed by the auditor. On the other hand, it is advisable to carry out a subsequent audit because as we explained in the previous point, due to the time, a hypothesis had to be established in the compliance tests.

Due to the characteristics of the audit, certain limitations have appeared, both of time and scope. Due to time constraints, we have only been able to do the audit for one

determined process; the main scope constraint has been the difficulty to access to all the information desired, so it is been necessary to establish some hypothesis.

The company had no problem in providing the necessary information in the course of the audit. It has been of help, to be able to improve the process of purchases and to establish new controls to obtain a good finalization. In addition, a remarkable recommendation has been the preparation of a manual of procedures of the department to avoid errors and at the same time for the future, as the company is growing, to facilitate the understanding to new members of the department.

This work has been a useful contribution for the company, so it'll be presented to them, having the future possibility of carrying out the audit for more areas and processes of the company, as for instance analysing the goods selling process.

5-REFERENCES

American Accounting Association (AAA) (1973), The Accounting Review. Available at: <http://aaahq.org/the-accounting-review> (accessed 11 March 2017)

Arens, A; Elder, J & Beasley,S. (2007). Auditoría. Un enfoque integral. 11 ed. México: Pearson.

Barquero, M. 2012. Manual Práctico de Control Interno, Ed. Profit, Barcelona.

Carias Santos, A; Estrada Martínez, I & Díaz, C (2011). Modelo de identificación y evaluación de riesgos desde el punto de vista de auditoría interna, aplicada al área operativa de la industria metal mecánica. Universidad del Salvador.

Chambers, A. (1992), Effective Internal Audits, How to Plan and Implement, Pitman Publishing,Boston,MA.

Chartered Institute of Management Accountants, (2005). CIMA Official Terminology. 2nd ed. OXFORD: CIMA, pp.5-6.

Committee of Sponsoring Organisations of the Treadway Commission (COSO) (2004), Enterprise risk management, Jersey City, NJ: Sponsoring Organisations of the Treadway Commission.

Committee of Sponsoring Organisations of the Treadway Commission (COSO) (1992), Internal Control, Jersey City, NJ: Sponsoring Organisations of the Treadway Commission.

Committee of Sponsoring Organisations of the Treadway Commission (COSO) (2013), Internal Control, Jersey City, NJ: Sponsoring Organisations of the Treadway Commission.

Del Toro, J. et al., (2005). Programa de preparación económica para cuadros. Centro de Estudios Contables Financieros y de Seguros. La Habana, Cuba

Hevia, E. (1989). Manual de auditoría interna, Enfoque operativo y de gestión. Ediciones Centrum Técnicas y Científic,

Institute of Internal Auditors (IIA) (1990), International Professional Practices Framework. Available at: <http://www.theiia.org/guidance/standards-and-guidance/ippf/definition-of-internal-auditing> (accessed 29 April 2017)

Instituto de Contabilidad y Auditoría de Cuentas de España (ICAC) (1991), Normas Técnicas de auditoría. Available at: <http://www.icac.meh.es/> (accessed 5 April 2017)

Koutoupis, A. G. (2005). Corporate governance and internal audit in Greece, Panteion University of Social and Political Sciences. In Third European Academic Conference on Internal Audit and Corporate Governance.

Mautz, R & Sharaf, H. (1971), La filosofía de la auditoría. Ediciones Contables y Administrativas. Número 6.

The Institute of Chartered Accountants of India (2007). Guide on Risk-based Internal Audit. ICAC Bhawan. New Delhi

6.ANNEXES

Annex1. QUESTIONNAIRE OF INTERNAL CONTROL ENVIRONMENT

1.Integrity and ethical values

3

1.1 The codes of behavior and other policies exist and they are in application.	3
1.2. The direction is a good example for the whole collective and it clearly indicates what is right and what is wrong.	2
1.3. Honesty and ethics prevail in the established policies while dealing with employees, customers, suppliers, insurers, competitors, investors, debtors and creditors in general, etc.	3
1.4. Corrective actions are taken in response to departures from the policies and procedures or to violations of the code of behavior. Such measures are transmitted internally to all staff of the organization.	4
1.5. Mechanisms to ensure proper processing of transactions are established.	3
1.6. There is commitment to fulfill the objectives of possible yields.	3

2.Professional competence

3

2.1. There are formal or informal job descriptions or other ways to describe the functions involving specific jobs.	3
2.2. Knowledge and required skills are analyzed to realise properly the work.	3

3.Control Committee

3,37

3.1. The Committee reviews the decisions made by management (eg strategic initiatives, major transactions), and it looks for explanations for past results (eg, budget variances).	4
3. 2. Committees dependent on the Council are established in cases which are justified by the need to pay more detailed or direct attention to specific matters.	4
3.3. The members have enough knowledge, experience in the business of the	4

entity and time to perform their functions properly.	
3.4. Meetings are celebrated with the financial and/or countable people in charge, internal and external auditors with the necessary frequency and opportunity.	3
3.5. Information is provided to members of the Council or the Committee enough and appropriately in order to allow the monitoring of the objectives and strategies of management, financial position and operating results of the entity and the conditions of significant agreements.	4
3.6. The most sensitive information, research and significant and unusual events are promptly evaluated by the Council or the Committee of Control.	3
3.7. It is established the form to demonstrate that Superiors must lead by example.	2
3.8. The Council monitors the actions which are made as a result of its findings.	3

4. Ambience of mutual confidence

3

4.1. The direction acts carefully and only acts after analyzing the risks and potential benefits of an operation that carries risks.	3
4.2. There is staff turnover in key functions, eg, operational, accounting, data processing, internal audit.	2
4.3. The direction has concern towards the data processing and accounting functions, as well as the reliability of the presentation of financial information.	4
4.4. The direction of the group often celebrates meetings with the subsidiaries	3
4.5. There are interaction between the principal administration and the operational one, particularly when they operate from remote geographically locations.	3

5. Organizational Structure

3,6

5.1. The organizational structure is appropriate and it has the capacity to provide the necessary flow of information to manage its activities.	3
---	---

5.2. The responsibilities and the expectations of the main directors are defined with respect to the activities of their areas of responsibility	4
5.3. The managers have the knowledge and the experience appropriate to cover the assigned responsibilities.	4
5.4. The organizational structure is modified when there are changes in circumstances that require it.	3
5.5. It has enough employees with leadership and supervisory capacity.	4

6. Allocation of authority and responsibility	4
--	----------

6.1. The responsibility is assigned and the authority is delegated to deal with organizational objectives, operational functions and regulation requirements, including the responsibility about the information systems and the authorizations to make changes.	4
6.2. The rules and procedures related to the control are the suitable for department heads and supervisors.	4
6.3. The entity has the necessary staff, knowledge and experience to carry out their mission.	4
6.4. There is correspondence with the delegation of authority in relation with the responsibilities assigned.	4

7. Staff policies and practices	3,2
--	------------

7.1. The policies and procedures for recruitment, training and promotion of workers have been defined	3
7.2. Workers are informed of their responsibilities.	4
7.3. Corrective actions taken in response to deviations in the policies and procedures approved are enough and appropriate	3
7.4. Staff policies are oriented towards the observation of the ethical and moral standards in the company	3
7.5. The verifications of the candidate records, referred to previous behavior or non-accepted activities by the entity, are enough and appropriate.	3

7.6. The criteria for worker retention, promotion criteria and techniques for gathering information related to the code of conduct or other guidelines for behavior are suitable

3

LEGEND

4 Points: Excellent, the entity complies 100%.

3 Points: Good. The entity complies 80%. There are some aspects to improve in the short term

2 Points: Regular. The entity complies 60%. There are some aspects to improve in the medium term.

1 Point: Deficient. The entity complies 40%. There are some aspects to improve in the large term

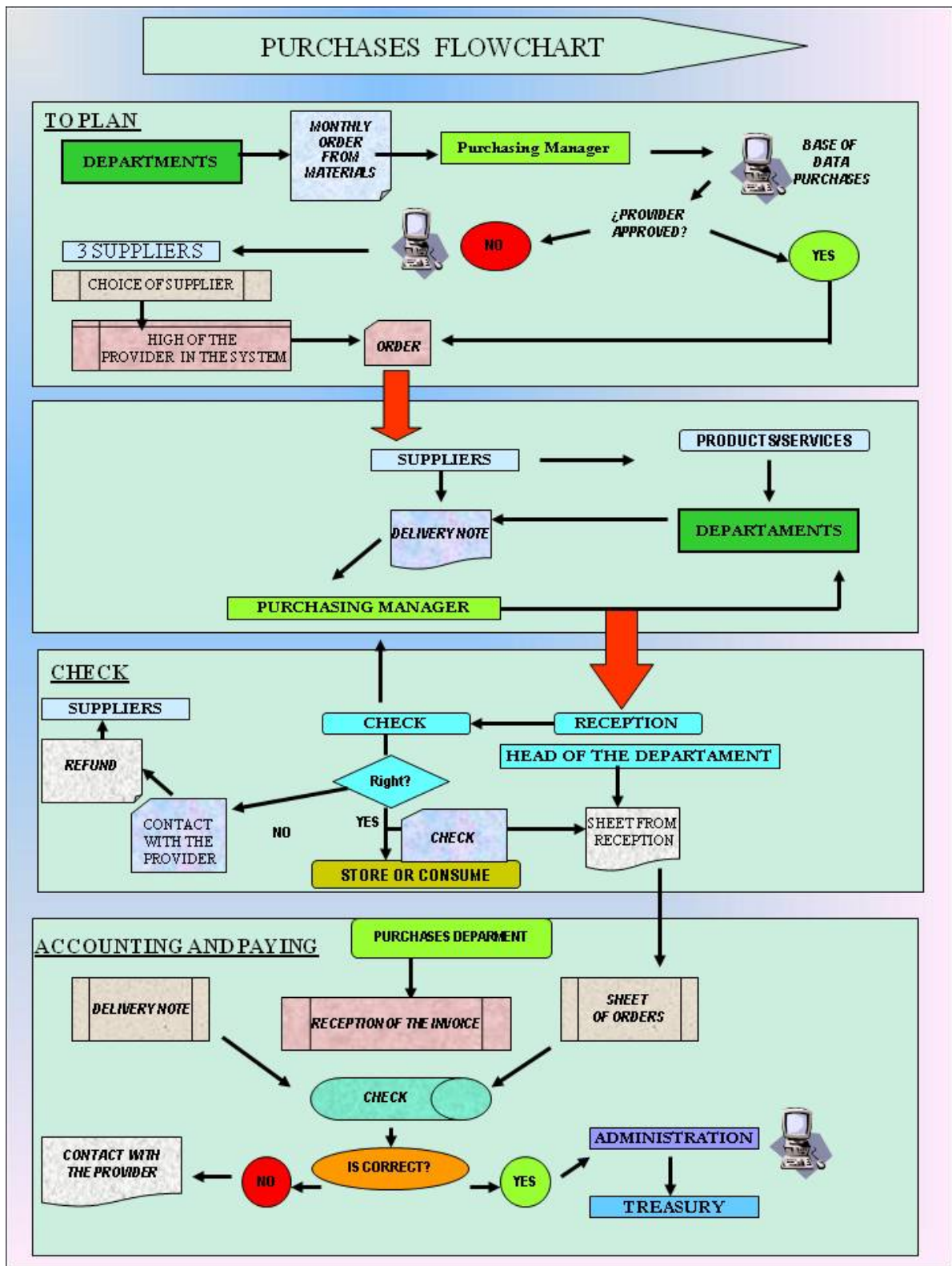
0 Point: Non-existent.

NOTE: If the question is "not applicable" is left blank.

Annex 2. RISK MANAGEMENT MATURITY QUESTIONNAIRE

QUESTIONS	ANSWER	LEGEND		
1. Are corporative objectives defined?	YES	2	YES	
2. Is a procedure for determining the risks defined and established ?	YES	1	PARTIALLY	
3. Is it defined a system of risk assessment?	YES	0	NO	
4. Are all risks assessed based on the procedure established?	YES			
5. Are risks managed through internal control systems?	YES	Conclusion on Risk Maturity		
6. Are there control mechanisms that evaluate the correct operation of control systems?	YES	Risk Naïve	0 - 7	
7. Are risks reviewed regularly by the organization?	YES	Risk aware	8 - 14	
8. Has the organization defined risk appetite through a scoring system?	NO	Risk defined	15 - 20	
9. Is the responsibility of workers in the identification, assessment and management of risks clearly included in their functions?	PARTIALLY	Risk managed	21 - 25	
10. Do managers ensure an effective risk management?	PARTIALLY	Risk enabled.	26 and above	

Annex 3. PURCHASES FLOWCHART



Annex 4. PURCHASES QUESTIONNAIRE

Company: Company A
Process: Purchases
Responsible auditor: Maria Falquet Torres
Interviewe : Laura García
Date: 12/05/2017

Nº	QUESTION	YES	NO	N/A	COMMENTS
1	Does the company have a Procurement Procedures Manual of purchases?		x		
2	Are there specific policies to carry out the processes and activities?		x		
3	Are the products and the requirements requested from the suppliers defined in a document?		x		
4	There are techniques used to determine that procurement has the best relationship between cost and utility?		x		
5	Are several price quotes requested from suppliers?	x			
5a	Are they kept in a registry in the system?	x			
5b	Are written explanations required in cases where no quotes were requested, or the purchase was made to those who did not offer the lowest quote?	x			
6	Are Purchase Orders prepared for all Acquisitions?	x			
7	Are the Purchase Orders authorized?	x			
8	Are there rules on purchase authorizations based on the amount or limit of the authorization?	x			
9	Are the purchase prices reviewed by a non-purchasing official in order to determine if		x		

	they were made at the most favorable prices and conditions for the company?				
10	Are special approvals required for certain purchases due to their class, quantity or other limitations?	x			
10a	Who controls?				Head of purchasing department.
10b	How often?				Annually.
11	The best option of the budgets for the purchase of goods is taken jointly between the responsible of purchase and the one of production?		x		
12	Can anyone introduce into the system unauthorized providers ?	x			
13	Are certain authorized suppliers revalued by applying for new offers? How often?	x			Annually.
14	Does the system allow orders to be made to suppliers that are not registered in the system?		x		
15	Are inventory levels checked for each product that is placed in an order?		x		
16	Is it checked that there are no pending orders to be received with a certain age?	x			
17	Are the volumes purchased from major suppliers reviewed and studied?	x			Yes, in order to negotiate with them.
18	Are the average purchase prices revised for each product reference compared to the previous year and with the evolution of the cost of materials?	x			
19	Are rotational inventories made from time to time? Are they made by people outside the daily management of the warehouse?	x			They are not made by people outside the warehouse.

20	Is the purchase cost automatically accounted for by the amount resulting from the input quantities and the prices of the order placed to an account of invoices pending receipt?		x		
21	Is the supplier required to refer to the order number on your invoice?		x		
22	Is there segregation of duties between the purchasing and the treasury?	x			
23	Is there adequate coordination between procurement and accounting?	x			
24	Do purchase orders contain information on all the desired requirements? Is the methodology defined for the purchase requirements?	x			
25	Is there a correlation between physical and digital information?		x		

Annex 6. RECOMMENDATIONS

EVENT	Nº	AUDIT TEST	RECOMMENDATIONS
The selection of the best option of the offers obtained by the purchasing department is not taken jointly between the responsible of purchases and the one of production.	1	Check the selections of offers for the purchase of a product and check that it is chosen jointly between the two through a meeting.	Make all the selections of best offers jointly between the two responsible for a more appropriate production and with more quality.
Not only the authorized person in the purchasing department can enter suppliers in the system database, they can also enter it from the accounting department.	2	Check how many times a vendor has been introduced by the accounting department to see if it is necessary to take action and change the process of introducing suppliers to the system.	Attempt that the system can limit people to register new providers in the database. And consider how to appoint two responsible for the introduction of suppliers, which are one of purchases and the other accounting, who would be the person Who is posting invoices. To do this, prepare a document shared between the two people so that at all times they inform of the providers that have introduced and certain characteristics about these.

<p>The average purchase price is not checked in each order made and for each product reference, comparing them with the budget, with the previous year and with the evolution of the cost of materials.</p>	<p>3</p>	<p>A check on this is not necessary, because the risk is in the area of risk appetite. But if it is interesting to make a recommendation.</p>	<p>Make a monthly report by company and product group, of the purchases made comparing the volume and price information with the budget and with the previous year.</p>
<p>It is not reviewed that the stock levels for each reference being purchased are reasonable to the needs.</p>	<p>4</p>	<p>It will be reviewed for a sample of purchases of products made, that have been reviewed before the purchase the stocks, because it could cause an excess of stock and space problems would occur.</p>	<p>The function of the controls causes the risks to be mitigated. The process must be monitored, as well as to verify the absence of errors. And prepare the system so that when an order is placed an informational row in the system indicating the stock level of the product, this will save a lot of time to the purchasing staff that has to check the stock level to be able to review the orders.</p>
<p>Inventories made during the year, are not made by people outside the daily management of the warehouse.</p>	<p>5</p>	<p>A check on this is not necessary, because the risk is in the area of risk appetite. But if it is interesting to make a recommendation.</p>	<p>That inventories made during the year are carried out by people outside the warehouse management, that is to say by two more responsible areas related to this task. One of those responsible should be the person in charge of making purchase orders.</p>

<p>The cost of purchases made is not automatically accounted for the amount resulting from the inputs quantities of product entries and prices of the order placed, with an account of invoices pending receipt.</p>	6	<p>The control is not set due to its cost.</p>	<p>Looking to the future, a recommendation would be to implement a system of bar codes in which the amounts of product entries and the prices of said order to an account of invoices pending reception were recorded directly in the system.</p>
<p>Personnel who enter invoice data into the system do not associate it with an order (normally the supplier is required to refer to the order number on their invoice), but suppliers are not required to refer to Order on the invoice. So the system does not compare that the invoiced amounts match those received, likewise does not verify that the prices of the invoice are those authorized in the system or those included in the order.</p>	7	<p>Check that the invoices are included with the order number.</p>	<p>Require the supplier to indicate the order number on the invoice.</p>

<p>There is no segregation of duties between the people responsible for the purchasing process and the treasury.</p>	<p>8</p>	<p>Check that the roles of purchasing and treasury have been separated.</p>	
<p>There is no correlation between physical and digital information.</p>	<p>9</p>	<p>At the end of next month make a comparison between paper documents and those that have been introduced to the database.</p>	<p>It is recommended to monitor the entire process and verify that no errors are occurring. For it will be necessary; Make monthly revisions and try to delete the paper format, registering everything in a system database.</p>

Annex 6. AUDIT REPORT

INTERNAL AUDIT REPORT

The classification of the report are exposed below:

- 1. PRE-CLARIFICATIONS**
- 2. AUDIT OBJECTIVE**
- 3. SCOPE AND METHODOLOGY OF WORK**
- 4. LIMITATIONS OF THE SCOPE**
- 5. AUDIT APPLIED PROCEDURES**
- 6. IMPLEMENTATION OF THE RECOMMENDATIONS**
- 7. OPINION OF THE AUDITOR**

1. PRE-CLARIFICATIONS

√ This time it was the first internal audit performed to a company process, so the analysis started from the beginning without any information on which to rely on previous audits.

2. AUDIT OBJECTIVE

√ Carry out an evaluation of the company's risk approaches, so that it can provide a consulting activity, and maintain an effective internal control in the company.

3. SCOPE AND METHODOLOGY OF WORK

√ The approach used was the internal control COSO (1992) and its subsequent updating COSO (2013).

√ The internal audit will focus on a specific process: purchase of goods.

√ The audit is duration was established to be of two and a half months due to the characteristics of the company and the selected process. Therefore, internal audit began in March and ended in late May with the results' presentation.

√ The internal audit is carried out by María Falquet Torres.

4. LIMITATIONS OF THE SCOPE

√ Only the internal audit of a process has been performed, due to the short time to perform it.

√ Two hypotheses have been made, in the absence of information and time. One of them has been the levels of definition of risk and the other the audit test performed on the company, because there was not enough time.

5. AUDIT APPLIED PROCEDURES

The procedures followed by the auditor are:

√ To gather the necessary information of the company and of the process of purchases.

√ The risks of the process of buying goods through the application of techniques are identified.

√ The risks identified by the auditor are assessed.

√ The recommendations are made.

6. RECOMMENDATIONS

√ A recommendation that will help the company a lot is to have to establish a manual of procedures of the purchasing process, in addition to having to modify certain procedures of the process in order to improve the operation of the purchasing department.

√ The most important recommendation is the segregation of functions between the responsible for purchasing and treasury.

√ Annex 6 shows the recommendations table, which is composed of the identified event, the audit test hypothesis and the recommendations for each identified event. The audit tests will be carried out in the next phase, since for a matter of time they could not be performed.

7. OPINION OF THE AUDITOR

√ The auditor's opinion is favorable.

√ The company has good risk management.

√ In the recommendations table, the most pertinent ones that have to be implemented by the company have been exposed.