US CMA PART 1

Section A – Financial Reporting Decisions

Section B – Planning, Budgeting, Forecasting

Section C – Performance Management

Section D – Cost Management

Section E – Internal Controls

Section A

Financial Reporting Decisions

What are Financial Statements

A Collection of Reports

Prepared periodically

Reflecting the Effect of the **Financial Transactions**

End result of the Accounting Process

Balance Sheet

1. Statement of Assets and Liabilities
2. Ascertain the financial position

    What the business owns

    What the business owes

    Owners' Equity

3. Assets - Liabilities = Owners' Equity

Cash Flow Statement

Statement of Cash inflows and outflows

Cash flows from Operating Activities

Cash flows from Investing Activities

Cash Flows from Financing activities

General Purpose Financial Statements

General Purpose Statements

Prepared in conformity with US GAAP (Framework)

Transparency , Reliability and Adequacy

Consistency and Comparability

Reasonable knowledge of users

Discontinued Operations

Part of business that is discontinued/to be discontinued

No cash flows from this operation in future

No significant future involvement of the company in operation

Discontinued operations are shown net of tax.

Extraordinary items

Material items

Unusual in nature

Infrequent in occurrence

Fire, Flood, Government regulation

Each item to be shown separately

Comprehensive Income– Presentation

US GAAP	IFRS
In a single statement of comprehensive income, or	In a single statement of comprehensive income, or
Using a separate profit and loss statement & a statement of comprehensive income, or	Using a separate profit and loss statement and a statement of comprehensive income,
Within the statement of changes in equity	

Financing Activities

Issue of stock / Capital Contribution

Issue of securities

Buy back of stock

Loan taken

Repayment of Loan

Dividend payment

Statement of Changes in Equity - Components

Common stock

Preferred stock

Additional paid in capital

Paid in Capital

Retained earnings (Net income/loss)

Treasury Stock

Owners' Equity = Assets – Liabilities

Revenue Recognition- Point of Sale

Sale of products	On date of sale/delivery
Sale of services	After performance
Loss/Gain on sale of assets	As on date of sale
Income from use of asset	On time or use basis

Cost Recovery Method

Most conservative method

Credit sale with no basis to determine collectibility of future payments

Recognition of profit only after entire cost is recovered

No transfer of title of goods

Rarely used, requires disclosure

Long Term Contracts

Construction Contracts

More than a year to complete

In which period will revenue be recognized

Accrual Concept

Expense for the year, whether paid or not

Income for the year whether received or not

Debtor and Creditor

Prepaid and Outstanding expense

Accrued/Outstanding income and Unearned Income

Cash Equivalents

Securities with a maturity of 3 months or less **at time of issue**

Can be easily converted to cash

With no risk of loss in value

Restricted Cash - not a cash/cash equivalent

Not a part of Cash and Cash Equivalent

Will be shown separately in Balance Sheet

Maybe Current or Non-Current

Restriction may be Contractual or Voluntary

Reason for restriction must be disclosed in the notes to FS

Valuation Account

Valuation account is usually a balance sheet account

used in combination with another balance sheet a/c

to report the carrying amount of an asset or liability

E.g. Allowance for Doubtful Accounts.

% of Receivables -Ageing Schedule

An accounting table

Shows the relationship

Between a company’s bills and invoices and their due dates.

May be used to arrive at the balance of allowance required

Non Trade Receivables

Receivables other than from sale of goods/services

Advance to employees, Insurance claim , Tax refund etc

Usually current

Evaluate at the end of the year

Non Trade Receivables to be reported as a separate item

Specific identification method

Reflects actual physical flow of goods

Most accurate

Not very practical

Can be used only when goods are not interchangeable

Specific items for specific project

What are Intangible Assets

Long Term Resources

No physical presence

Cannot be touched

Derive value from intellectual or legal rights

Accounting for Intangible Assets

Initial recording of the asset

Amortization of the cost of the asset (if finite life)

Testing and adjusting for impairment (if infinite life)

Disclosure

Debt Securities

Held for Trading	Held for selling immediately to generate short term profits
Held-to-Maturity	Purchased with the intention of holding till maturity
Available-for-Sale	Not classified as Trading or Held-to-Maturity

What is a Warranty

A promise by seller to buyer

If product sold is found defective within specified period

Will be repaired / replaced

Free of charge

Sales Warranty - Revenue Recognition

Revenue received is deferred over life of warranty

Usually straight line basis

If costs are incurred on other basis, revenue recognition accordingly

Recognition may begin only after expiry of manufacturer’s warranty

Unearned revenue is liability

What is Deferred Tax

Accounting Profit as per Accounting Standards

Taxable Income as per Tax Laws

Could be a difference
(due to difference in timings of revenue and expense)

Deferred Tax Asset or Deferred Tax Liability

Only if the differences are temporary

Identifying a Finance Lease

Any one of the following conditions needs to be satisfied:

(For the lessee)

a) Transfer of ownership at the end of lease
b) Lease contains an option for a bargain purchase
c) Lease term is 75% or more of the life of the asset
d) PV of lease payments is 90% or more of the FV of asset

No par Stock

No-par stock that has no stated value, no par value

Recorded in a single account at the selling price

No additional paid-in capital recorded

Treasury Stock

Treasury stock is reported as a reduction of stockholders' equity

Treasury stock (shares) have no voting or dividend rights. Reacquired shares are accounted for by

either the cost method or (more popular)

the par value method.

What are Retained Earnings

Accumulated profits of the organization

Usually available for distribution as dividend

Dividend distribution decreases retained earnings

Retained earnings may be appropriated,

- Reserve or restricted retained earnings
- May be de-appropriated later

Section B

Planning, Budgeting, Forecasting

What is Strategic Planning

Systematic Process of Visualising the Goal

Defining the Direction that the organization will move in

Assessing the Environment

Systematically allocating resources

Provide plans to give the organization a competitive advantage

Organization Values

Foundation of the Organization’s Culture

Behaviour of employees in the conduct of business

What does the organization care about ?

Employees’ values should be aligned

Values alignment helps the organization as a whole to achieve its core mission.

Maybe unwritten informal policies or code of conduct

SWOT Analysis

SWOT analysis is a tool

Gives an overall view of an organization's strategic position

Highlights the need for a strategy

To fit between the internal capability (strengths and weaknesses) and the external situation (opportunities and threats).

Generating conversion strategies.

PEST(LE) Analysis

Helps to analyse external environment that influence the organization

Environment may be outside organizational control

Need to understand impact of external environment on organization

PESTLE analysis provides a framework to investigate the environment

Questions can be raised on each of the factors in the analysis

And their implication on the organization

Porter’s Five Forces Industry Analysis

Important tool for assessing the attractiveness of an industry

Works by looking at the strength of five important forces that affect competition…..

A way of assessing the balance of power in more general situations.

How then to move the balance of power in favour the organization

Differentiation Strategy

Developing a product or service that is perceived to be different

Unique attributes that are valued by the customer

A premium price may be charged

Customers remain loyal

Good research, continuous innovation and development required

Effective sales , marketing and brand management required

Focus Strategy

Concentrates on a narrow segment and within that segment achieves a cost advantage or a differentiation

Cost Focus or Differentiation Focus

Believes that the needs of the group can be better serviced by focussing entirely on it

Build strong customer loyalty and thus discourage competition

A premium price may be charged

BCG Growth Share Matrix

Was created by Boston Consulting Group (BCG) in 1970

To help organizations analyze their portfolio of products/business lines

So that they can allocate resources appropriately

Products/business units are ranked on the basis of their relative market shares and market growth rates

Placed into one of the four quadrants

Organizational culture

Percolates from top to bottom

Partly influenced by the organizational structure

Maybe “Innovative” , “Competitive”

“Stable and Traditional” , “Collaborative”

Budget

A proposed plan of action expressed in quantitative terms

It covers a defined period of time

Suggests allocation of resources to achieve goals and objectives

Can cover financial and non financial aspects of the plan

Helps to align the company's resources with its strategy

Serves as a control tool to evaluate performance

Includes planned revenues, expenses, assets, liabilities & cash flows.

Budget Slack

Deliberate overestimation of expenses or

Deliberate underestimation of revenues

Occurs usually with participative budgeting

Also occurs when there is uncertainty of the future results

Top management needs to be very alert while approving budgets

Cost Standards

Cost standards are established to control costs

Cost standards are laid down for each operation

May be based on historical data

May be based on engineering studies

Standards costs are used to make budgets

Standards may be revised based on changes in circumstances

Incremental Budgeting

Traditional budgeting method

Current budget or performance is taken as base

Incremental amounts may then be added

Would take inflation also into account

Zero Base Budgeting

Start from scratch

Need to justify every penny being spent

Need to justify every activity being performed

Previous budgets are ignored

Objective is to ensure optimal allocation of resources to the areas that

need them the most

Flexible Budgets

Prepared for different levels of activities

Considers the effect of fixed and semi variable costs

Essential when a high degree of variability in sales and production is

expected

Can be easily adjusted according to volume of production

Project Budgeting

Separate from other elements of the company

Duration of budget depends on duration of project

Master budget for a project

Certain overheads of the company get allocated

A possibility that the project staff are utilised by the company

Capital Budget

Long term Budget

Expenditure for property, building, machinery

Advance planning helps to ascertain finance requirements

Incorporated into the annual budget

Additions to property, plant etc will be reflected in the budgeted B/S

Purpose of Pro forma Financial Statements

A part of the planning process

Can ascertain cash position

Facilitates compliance with Strategic Objectives

Estimates the effects of changes in the key assumptions

Helps to determine dividend policy

What is Regression Analysis

Regression Analysis is a statistical tool

Used to analyse the strength and direction of the relationship between

two or more variables

Coefficient of correlation (R)

Numerical measure of the relationship between two variables

Strength of relationship

Direction of relationship (+ve or -ve)

"R" (or "r") lies between -1 and +1

Regression line

Regression line is the line of best fit for a given sample

It represents the general trend

The line can be represented by the equation

$y = a + bx$ or "y- hat" represents the predicted variable

Residual = Actual value - Predicted value

Multiple Regression

The simple regression equation measures the relationship between two variables (independent and dependent variables)

A multiple regression model is similar to a simple regression model except it has two or more independent variables.

Not only advertising, but economy, competition etc. would also be used to help determine a change in the dependent variable (sales).

Learning Curve

Learning curve model is a mathematical/graphical portrayal

It reflects the decreasing rate of increase in labour time with experience.

The cumulative average time per unit produced is assumed to fall by a constant percentage every time total output of the unit doubles.

It takes less time to complete each additional unit a firm produces.

Also known as Experience curve, Improvement curve or Progress curve.

Expected Value

An expected value is a weighted average of all possible outcomes.

It is computed by multiplying the value of each possible outcome (x) by the probability of that outcome (p), and summing the results.

Probability

A chance that a certain event will occur

Potential values ranging from 0 to 1
From “the event will not occur” to “the event will definitely occur”

The total of all the probabilities = 1

Section C

Performance Management

Centralised and Decentralised Organization

In a centralised set up, individual managers have little power

They do not have the freedom to take independent decisions

In a decentralised set up, decision making is left to individual managers at different levels

Managers are made in charge of certain portion of the business They are then responsible for that portion of the business, for that responsibility centre

What is a Responsibility Center?

In a decentralised set up, Responsibility Center is an organizational unit…

(a division, a segment, a subunit of an organization)

Which grants responsibility of the centre to a manager

Who is responsible for the unit's activities and results; its costs, profits, revenues or investment

A responsibility centre is also called an **SBU** (Strategic Business Unit)

Responsibility Accounting

Responsibility Accounting is method of measuring the effectiveness of Responsibility Centers

Managers of the Responsibility Centers are responsible for the results and effectiveness of these centers

Responsibility reports show the performance achieved by various responsibility centres.

Deviations from the budgeted performance should be reported at the earliest so that corrective action may be taken for the future.

Operating Segments

Operating segments are:

Subunits of a company that generate their own revenues and incur expenses

Viewed as a separate unit by management from a decision-making perspective

And for which separate financial information is available

Reporting segments may be divided along product lines, geographical areas or other meaningful segments

Segment Reporting

Segment reporting is intended to give information to investors and creditors

Regarding the financial results and position of the most important operating units of a company

To use as the basis for decisions related to the company.

Under US GAAP, all publicly held companies must report on operating segments in the Disclosures to Financial Statements

Common Costs

Some fixed costs cannot be traced to any particular segment of the business

They are common costs, costs that would be incurred even if a segment were to be discontinued

Common costs may be allocated on an arbitrary basis since cause and effect may be difficult to establish…..

What is Transfer Pricing ?

When one subunit of a company transfers goods or renders services to another subunit, it may charge a price for the same. This price is called a Transfer Price.

If Division A transfers goods to Division B for a price, such "Price" is "Revenue" for Division A and "Cost" for Division B.

Thus operating revenues of both divisions would be affected

Of course, the profits of the company remain the same ...

Variance Analysis - Introduction

Each organization has its strategic objectives

Short term operational objectives - “Budget”

Difference between actual performance and budgeted performance - “Variances”

Variances may be Favourable or Unfavourable

Performance Management includes activities which ensure that goals are consistently met in an effective and efficient manner

“Variance Analysis” is the quantitative investigation of the material differences between actual and planned behaviour

Standard Cost

Standard costs are computed at the beginning of each period

Standard costs are estimates of what the management thinks the costs and revenues should be for a unit of output

Based on the standard costs and demand estimates Standard (Static) Budget is drawn

Standard budget would depend on the level of activity

Material Purchase Price Variance

Material Price Variance is usually applied on material used/ consumed.

If Material *Purchase* Price Variance is required to be computed, we use the purchased quantity instead of the quantity used.

Usually, Material Price Variance refers to Material Price Usage Variance

Variable Overheads

Variable overheads change as the level of production changes

All expenses, other than labour, that changes with the number of units is a variable overhead

They cannot be identified physically with a product and therefore are indirect costs i.e. overheads

But they change with the number of units produced…, therefore they are variable costs

Power and other utilities, packing costs etc..

Fixed Overhead Variance

<u>Actual Fixed Overheads:</u>

Refers to the actual incurred overheads

<u>Budgeted Fixed Overheads</u>

Refers to the o/h as fixed at the beginning of the year. It is a static budget variance, but fixed cost is fixed… so no sales volume variance

<u>Applied / Absorbed Fixed Overheads:</u>

Refers to the overheads absorbed based on a standard rate per unit or based on the standard hours required for actual output

Market Variances

Market Size Variance:	Variance due to the difference in the estimated market size and actual market size
Market Share Variance:	Variance due to the difference in the estimated market share and actual market share

Section D

Cost Management

Cost unit, Cost object, Cost center

Cost Unit	a unit of product or service in relation to which costs are ascertained.
Cost Object	a product, a service, an activity or department for which costs are accumulated or measured
Cost Center	a location, person, item of equipment (or group of these) for which costs may be ascertained and used for the purpose of control.

Cost accumulation and cost assignment

Cost Accumulation

Collection of costs in an organized way

Cost Assignment

a) Tracing accumulated costs directly to the cost object

b) Allocating accumulated indirect costs to the cost object on some suitable basis

Irrelevant costs

1.	Sunk cost	Cost which has been incurred and cannot be recovered
2.	Committed cost	Cost which has been committed to be incurred
3.	Non controllable costs	Costs which are not within the control of the person/department (vary from situation to situation)

Actual Costing

Costs are recorded as actually incurred

Direct costs per unit are recorded as incurred

Indirect costs are allocated after computing actual overhead rates.

Therefore, there could be fluctuations depending on the quantity produced

Standard Costing

A standard cost is what a cost ought to be

Standards for direct and indirect costs are pre-determined

These standard rates are applied to the quantity actually produced

Standard cost is the standard cost for actual output…...

Blanket rate

Simple method of allocating overheads

Total estimated overheads / Total activity level

Single or Blanket rate of absorption

Not likely to be very accurate

Capacity and Level of Activity

Capacity refers to the ability of a company to produce a product/service, within a given period.

The level of activity would depend on the capacity levels

Huge capacity but less needs → high unused capacity cost

Less capacity than it needs → demands not being met

For computing overhead absorption rate, ***normal capacity*** is usually considered

Theoretical Capacity

Largest possible volume of output

No delays, no breakdowns, no repair maintenance hold up

Not attainable ; not realistic

If used to compute O/H absorption rate, the rates would be very low and there would always be under absorption

Practical Capacity

Currently attainable , more realistic capacity

Theoretical capacity *less* allowances for unavoidable delays/

interruptions…..

Does not consider expected demand / sales levels

Often used to compute O/H absorption rates…

More accurate product costs

Management is forced to think about unused capacity costs

Master Budget Capacity

Anticipated capacity for the next year or half year

Costs would vary depending on the level of activity

Used for current performance measurement

So different rates may be used for different purposes

Methods of Allocating Multiple Service Department Costs

Direct Method → Costs are apportioned directly to Production departments

Step Down Method → Costs of each service department is apportioned to all other departments in a sequential manner

Reciprocal Method → Assumes that the service departments mutually provide service to one another

Direct Method

Is the most commonly used method.

It is simple

Each service department costs are allocated only to the production departments on a suitable basis of allocation.

Not allocated to any service department

Step Down Method / Sequential Method

The department which provides greatest service is allocated to all the remaining departments - both production and service

Then the costs of the next service department is apportioned to the remaining departments

So S1 may provide service to S2 and S3 but any service rendered by S2 and S3 to S1 is not recognized

Reciprocal Method

Under this method the services rendered by each support department to other support departments is recognized.

Mutual services between support departments is recognized.

Computations are more complicated.

May use the Repeated Distribution Method or Simultaneous Equation Method.

Process Costing

Is used when standardised, continuous mass production is involved

Costs of each process is determined

Cost per unit = Total cost of processes / Units of output

Joint Products

Joint products have significant market values

Joint costs need to be suitably allocated

Inventory needs to valued with a reasonable amount of accuracy

Costs incurred after split off ----- further processing costs can be easily identified

E.g. Processing milk to get butter, cheese & cream

What is Activity Based Costing ?

A method of cost accounting system

To allocate indirect costs to cost objects

Based on the extent to which cost objects use activities that consume resources

More accurate allocation of overheads

Value Chain of a Product

Process by which raw materials are received and value added at every process to create a finished product and sell to customers

Objective: is to deliver maximum value for the least possible total cost and create a competitive advantage

Value Chain model as such was developed by Michael Porter

Life Cycle Costing

Costs incurred during the entire life of the product

Include the Design and Development costs, Operating costs, Support costs, Dismantling and Disposal costs ….

Many products incur high non production costs

Life cycle costs are compared with the expected revenues to determine the profitability of a product

Supply Chain

"A **supply chain** is a system of organizations, people, activities, information, and resources involved in moving a product or service from supplier to customer."

Supply Chain Management (SCM)

SCM is the management of materials, information and finances as they move in a process from supplier to manufacturer to wholesaler to retailer to customer.

SCM is the management of the activities of procuring raw materials, converting raw materials to FG and delivering that finished good to consumers.

Lean Manufacturing

Systematic method for waste minimization ("Muda")

Without reducing productivity

Simultaneously adding value

Value being any action or process that a customer is willing to pay for

Materials Requirement Planning (MRP)

MRP is an information system

To help production managers schedule and order raw material, components, sub-assemblies……

Items of dependent demand

Scheduling will depend on the required machine hours, machine capacity and available labour hours to meet sales forecast

E.g. in a computer assembling unit, monitors, key boards, motherboards etc…. may be items of dependent demand

Theory of Constraints

According to the TOC

Do not try to increase efficiency equally in all manufacturing processes

This might result only in accumulation of inventories (WIP) at different stages

It will not increase profitability

What is a Value Chain

Set of interdependent activities carried out by an organizations that add value to a product/service while converting input to output.

Manufacturing industry: Raw material is converted into finished product which has value to the customer

Retail Industry: Products are sourced, stored and made available to consumers sometimes with additional services of fitting rooms, testing the product etc….each activity adding value to the customer

Service industry: Time, knowledge, systems, equipment … are input to render services of value to their customers

Value Chain Analysis

Value chain is a set of activities that create value for customer

Adding value leads to competitive advantage

And hence greater profitability for organization

Competitive Advantage is an advantage over competition to generate greater revenues and greater profits

Process analysis

Step by step breakdown of the activities in a process

To improve understanding of how the process operates

Identify areas of process improvement

Through reduction of waste and increase of efficiency

Or opt for Process Re engineering

Business Process Reengineering (BPR)

Japanese had been very successful in the BPM…..

Small incremental changes over a period of several years had let the Japanese companies achieve a high level of efficiency

In the USA, BPR was introduced by Dr. Hammer and James Champy in the 1990s to cover this huge gap in progress

BPR advocated a fundamental rethinking and radical redesign in the business process.

Companies start with a blank sheet of paper and rethink existing processes to deliver more value to the customer.

Kaizen

Kaizen is recognized worldwide as an important pillar of an organization's long-term competitive strategy.

Kaizen is the practice of continuous improvement

By everybody, everywhere, everyday

Accumulation of small improvements over time lead to high quality and low costs

Activity-Based Management (ABM)

ABM describes management decisions that use activity based costing information to satisfy customers and improve profitability.

ABC is a measure of the costs & performance of activities,resources,& cost objects.

ABM focuses on the management of activities as the way of improving the value received by the customer and the profit achieved by providing this value

ABC designates and uses cost drivers for each activity

ABM analyzes these cost drivers for their effectiveness in defining the root causes of activity costs.

Total Quality Management

Management approach to long term success through customer satisfaction

Total organizational involvement in improving products & services, processes, and the overall culture

No one widely agreed approach

Benchmarking

Benchmarking --> continuous, systematic process of measuring products, services, & activities against best levels of performance.

Best levels of performance may be found either inside one's own organisation or in other competing organisations or in organisations having similar processes.

Benchmarking uses best practices as the standard for evaluating activity performance. The unit with the best performance for a given activity sets the standard. Other units then have a target to meet or exceed.

Accounting Process Redesign

Business Process Improvement entails not only production process improvement

The Accounting Function is also a process….

Accounting and Finance should be able to provide higher levels of service in transaction processing with fewer resources

The freed resources would be used in more value adding services like decision support and strategic analysis

Section E

Internal Controls

Definition of Internal Controls

Internal controls are procedures designed to provide reasonable assurance regarding achievement of an entity's objectives in 5 areas:

SCARE:

Safeguarding of assets

Compliance with applicable laws and regulations

Accomplishment of organizational goals and objectives

Reliability of financial reporting records

Efficiency of operations

Segregation of accounting duties

Segregation of duties (SoD) is a measure of internal control

It serves two purposes:

a) There is a review and a greater chance of locating error

b) Fraud may be reduced since it would require collusion of two or more people

Information System Controls

General controls relate to the general environment within which the the transaction processing takes place. They form a basis for effective application controls

Application controls are specific to individual applications

Designed to prevent, detect, correct errors during the input, processing or output stages

Application Controls

Controls that are specific to individual applications.

To prevent, detect and correct errors in transactions processed by accounting systems

Objective is to provide reasonable assurance that all processing is authorized, complete, and timely.

Feedback controls

Feedback controls provide information about system performance to ensure that it is working as desired

May consist of written or oral reports or it may be automated.

For effective corrective action, feedback information must be delivered quickly

Feedback controls are essentially diagnostic, measuring the difference between actual and desired results

Encryption

In a “Secret Key System”, each sender and a recipient has to have a separate set of keys

In a “Public Key/Private Key System”, a company that needs to receive encrypted data publishes a public key

It retains a “Private Key” with itself in order to decrypt the data

Routing verification

RV ensures that data is routed to the correct location

Transmitted data contains a header label identifying destination

When the transaction is received, the sending system verifies that the identity of the receiving computer matches the transaction's destination code

May have additional safeguards of echo check ……..

Firewall

Combination of hardware and software

Used to prevent unauthorised access from the Internet

Firewalls may also be used to prevent unauthorised access to specific systems like payroll….

Several controls may be contained in a firewall system

There could be an automatic disconnect after a specified number of wrong passwords

A report of Internet Usage is prepared including abnormal usage, attempts to make unauthorised entry….

Business Continuity Plan

A BCP must identify the exposure of the organization to internal and external threats

BCP refers to the processes and procedures that are carried out by an organisation

a) to ensure that essential business functions continue to operate with minimal disruption and
b) to protect the critical resources and assets of the organization in case of a disaster or emergency

Disaster Recovery Policies

A DRP focuses on recovering IT resources in case of a disaster

Disaster Recovery is the ability to restore data or applications in case the data centre or other infrastructure are damaged or destroyed

DRP is the most important element of a BCP

Internal Audit

"Internal auditing 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."

Internal Audit Charter

Internal Audit Charter is a formal document

Defines the IA activity’s **purpose, authority and responsibility**

Establishes the chief audit executive’s functional reporting relationship with the board

Authorizes access to records, personnel, and physical properties

Defines the scope of internal audit activities

Final approval of the internal audit charter resides with the board.

Defines the nature of assurance services /consulting services

Conflict of interest

“Conflict of interest is a situation in which an internal auditor, who is in a position of trust, has a competing professional or personal interest. Such competing interests can make it difficult to fulfil his or her duties impartially.

A conflict of interest exists even if no unethical or improper act results.

A conflict of interest can create an appearance of impropriety that can undermine confidence in the internal auditor, the internal audit activity, and the profession.

A conflict of interest could impair an individual's ability to perform his or her duties and responsibilities objectively.”

Internal Assessments

a)**Ongoing** monitoring of performance of the internal audit activity.

Should be a part of the routine policies and practices of the iaa

Part of the daily supervision, review and measurement of the iaa

Uses processes, tools, and information required to evaluate conformance with the Code of Ethics and the Standards.

b)**Periodic** self-assessments or assessments by other persons Such persons should have an understanding of the IPPF

External Assessments

Either (a) through a full external assessment, or

(b)a self assessment with independent external validation

Assessor/assessment team should be qualified and independent

Should be conducted at least once in 5 years

Must conclude on conformance with Code of Ethics and Standards

May also include operational or strategic comments.

Performance standards

Describe activities and indicate appropriate levels of quality

- Managing the internal audit activity
- Nature of work
- Engagement planning
- Performing the engagement
- Communicating the results
- Monitoring progress
- Communicating the acceptance of risks

Financial audit

A financial audit conducted by an internal auditor is forward-looking

The auditor assesses the adequacy of internal controls as they relate to financial activities.

The nature, timing, and extent of substantive testing will depend on the auditor’s assessment of the amount of control risk and the credibility of assertions regarding the company's transactions.

Details of account balances, analytical procedures, transactions, and the physical security of assets etc are looked into

Audit risk

Audit risk (or residual risk) is the risk that an auditor may issue an unqualified report due to the auditor's failure to detect material misstatement either due to error or fraud

Corporate Governance (CG)

CG refers to the system by which a corporation is directed and and controlled

Governance provides the structure through which corporations pursue their objectives while considering the social, regulatory, and market environments in which they operate……

CG specifies the rules and procedures for making decisions in corporate affairs

What are the rights and responsibilities of the participants in a corporation ?

Pre numbered forms

Pre numbered documents are an one of the tools to maintain internal control

It establishes a control over completeness of information

If cash receipts are pre numbered and some of them go missing, it could indicate that someone is receiving money and issuing a receipt which is not being recorded in the books.

Invoices, checks, goods received notes etc can be pre numbered so that it is easy to identify if it is not in sequence

All pre numbered documents must be preserved, if cancelled the cancelled form should be retained.

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US CMA PART 1

For more details –

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https://meraskill.com/cma

www.youtube.com/meraskill