

# **Internal Control and Fraud Detection**

---

Distributed by The CPE Store  
[www.cpestore.com](http://www.cpestore.com), 1-800-910-2755

# Table of Contents

---

<b>Chapter 1 – The Principles of Internal Control</b> .....	<b>1</b>
Learning Objectives .....	1
Introduction.....	1
Internal Control Systems.....	1
The Definition of Internal Control.....	1
Limitations of Internal Controls.....	2
Internal Control Frameworks.....	2
2013 COSO Framework.....	2
The GAO Green Book.....	10
Types of Controls.....	14
Directive Controls .....	14
Preventive Controls .....	14
Detective Controls .....	15
Corrective Controls.....	16
The Concepts of ICFR .....	16
Integrating Controls over Information Systems .....	17
IT General Controls .....	17
IT Application Controls.....	18
Considerations Specific to Smaller Entities.....	20
Cost-Benefit Relationships.....	21
Cost-Benefit Analysis.....	21
Cost-Effectiveness Analysis .....	22
Review Questions.....	23
Review Answers .....	25
<b>Chapter 2 – Management Assessment of Internal Controls</b> .....	<b>27</b>
Learning Objectives .....	27
Introduction.....	27
Understanding the Sarbanes-Oxley Act Rules.....	28
Enhanced Financial Disclosures (Section 404).....	28
Management’s Internal Control Report.....	29
The Role of Independent Public Accountants .....	31
Corporate Responsibility (Section 302) .....	32
Other Key Principles .....	33
Identification of Risks and Controls .....	34
Step 1: Selecting the Control Framework .....	34
Step 2: Defining Control Objectives.....	35
Step 3: Addressing and Monitoring Risks .....	37
Step 4: Establishing Controls .....	40
Assessment of the Adequacy of Controls .....	41
Determining Key Controls .....	42
Evaluating the Effectiveness of Controls .....	43
Evaluation of Control Deficiencies.....	47
Step 1: Understanding the Nature of the Deficiency .....	47
Step 2: Assessing the Likelihood of a Misstatement .....	48
Step 3: Considering Compensating Controls .....	49
Step 4: Determining Classification of Deficiencies .....	49
Step 5: Reporting Assessment Results .....	50
Documentation of Effective Controls .....	51
Identification of Control Gaps.....	53
Illustration of Potential Internal Control Weaknesses and Compensating Controls: Accounting and Financial Reporting.....	55
Review Questions.....	57
Review Answers .....	58

Table of Contents

<b>Chapter 3 – Audit of ICFR Integrated with Audit of Financial Statements .....</b>	<b>61</b>
Learning Objectives .....	61
Introduction.....	61
Audit Objectives and Scope .....	61
Relevant Standards .....	62
Auditing Standard No. 2201 .....	62
Statement on Auditing Standards 130 .....	62
Planning the Audit.....	63
Using a Top-Down Approach .....	64
The Key Concepts .....	64
Sample Audit Programs .....	66
Assessing the Risk of Fraud.....	78
Characteristics of Financial Statement Fraud .....	78
Brainstorming Sessions .....	79
Testing Controls.....	82
Testing Design Effectiveness .....	82
Testing Operating Effectiveness.....	82
Relationship of Risk to the Evidence Obtained .....	82
Evaluating Control Deficiencies.....	83
Examples of Significant Deficiencies and Material Weaknesses .....	84
Responding to Misstatements Caused by Fraud .....	85
Reporting Audit Results .....	86
Types of Audit Opinions .....	86
Audit Matters .....	87
Other Considerations .....	90
Considerations Specific to Smaller, Less-Complex Entities .....	90
Considerations of Financial Information Systems .....	90
Management Written Representations .....	92
Communication of Certain Matters .....	92
Use of the Work of Internal Auditors or Others .....	92
Review Questions.....	94
Review Answers .....	96
<b>Chapter 4 – Fraud Prevention and Detection .....</b>	<b>99</b>
Learning Objectives .....	99
Introduction.....	99
Definition of Fraud .....	99
Fraud Awareness.....	99
Basics of Fraud.....	99
Types of Fraud .....	104
Forensic Accounting and Auditing .....	112
Fraud and Perpetrators.....	113
The Fraud Symptoms .....	113
Recent Cases in Corporate Fraud.....	115
Fraud Prevention and Detection.....	117
Fraud Risk Assessment .....	117
Techniques for Fraud Prevention .....	119
The Use of Technology for Fraud Detection .....	127
Review Questions.....	130
Review Answers .....	132
<b>Appendix A – Example of Management Report.....</b>	<b>135</b>
<b>Appendix B – Section 404 Management Compliance Checklist.....</b>	<b>137</b>
<b>Appendix C – Financial Reporting Controls and Information Systems Checklist—Medium to Large Business.....</b>	<b>139</b>
<b>Appendix D – Computer Applications Checklist—Medium to Large Business .....</b>	<b>153</b>
<b>Glossary.....</b>	<b>157</b>
<b>Index .....</b>	<b>161</b>