

Chapter-1 Overview of Auditing

Assurance service

- > is an Independent Professional service that improves the quality of Info. for decision makers
- > it is information reliability enhancement service performed by Auditors (CPA's) or others.

Categories of Attestation service

- * Attestation is a type of Assurance service in w/c the Practitioner engage in subject matter
Eg. - to provide report on internal control. / specific matter
- * Attestation provide info at its reliability.
- * There are 5-categories of attestation service:-
 - a). Audit of F/statement
 - b). Attestation of Internal Control over Financial Reporting.
 - c). Attestation about financial forecast
 - d). Attestation service on IT
 - e). Other Attestation services

forms of Attestation service

- 1). Examination (Audit): designed to provide high degree assurance
- 2). Review: designed to provide limited assurance
- 3). Agreed Procedures: designed to perform certain procedures for specified party.

Non-Assurance services

→ These are not Info. Quality enhancement services, simply they may be the FF:-

1. Acc'g and Book keeping Service
2. Tax Service
3. Mgt Consulting Service

Relationship Among Auditing, Attest and Assurance

<u>Service</u>	<u>Value Added to Info</u>	<u>Definition</u>
1). Auditing	• Reliability • Credibility	• A Report on Examination of F/statements for a client
2). Attestation	• Reliability • Credibility	• A Report on subject matter, that is a responsibility of others
3). Assurance	• Reliability • Credibility • Relevance • Timeliness	• A Professional service that will improve the quality of Info. or its contents for decision.

(x). We are in the age of Info Now, so every one need fair & dependable Info, Therefore Auditors provide opinion on the fairness and dependability of financial statements.

(x). "Auditors" are individuals of Professional competence and Integrity who can tell others whether the Financial Info. is fair, complete and dependable.

- * "Auditing" is a work performed by an auditor to enable him/her to express an opinion on whether the F/statments are prepared according to the standards (IFRS, GAAP).

Why Auditing

- > To Perform Attest for: meaning to provide opinion as to the fairness and dependability of F/stat.

* Fairness = if it is prepared acc. to acc'g principles

* Dependable = if it isn't biased.

Contribution of Independent Auditor

- > Accountants Report aren't credible for outsiders such as:- stockholders, creditors, Gov't b/c accountants are under the control of the mgmt. (they may bias the F/stat.)

- > Therefore Independent Auditors give the F/stat. credibility. (Reliability).

* An Auditor doesn't guarantee that the F/stat. are correct, BUT gives an opinion as to whether the F/stat. are free from material misstatement.

* Thus an auditor only gives Reasonable assurance Not Absolute Assurance b/c of:-

- 1). Audit is conducting by taking sample
- 2). Auditors Rely on Internal Control systems

Features of Auditing

1). Systematic Approach

- Is purposeful, logical and based on structured discipline as to decision making.

2). Obtaining and Evaluating Evidence

- Involves a process of obtaining & evaluating evidence that guides the auditor's decision.

3). Obtaining the Assertion of the Mgt

- Assertion means claim, so we need to collect claim about economic actions & events.

4). Establish Standard (Criteria)

- Obtain on w/c standard does the F/stat. established

5). Compare the Assertion with the established criteria

6). Communicating the Result (giving opinion).

Need For Audit

- A Tool For Control
- Enhancing credibility of Info.
- Improving Economy and Efficiency
- It is mandatory Requirement in most countries.

Limitation of Audit

- * It's opinion is based on sampling
- * It can't Predict future events
- * It may fail to detect fraudulent txns
- * Provides Reasonable Assurance not Absolute
- * Evidence obtained is Persuasive rather than conclusive.

Objectives of Auditing

a). Primary Objective

- To give opinion as to the established criteria.

b). Secondary Objective / Incidental Obj.

- Detection and Prevention of fraud
- Detection and Prevention of Error.

The Diff Btwn Acc's and Auditing

Comparison

Accounting

Auditing

1). Primary Responsibility	• Preparation of F/statments	• Auditing of F/statments
2). Criteria in discharging responsibilities	• GAAP, IFRS	• GAAS, IAS
3). Its Nature	• Constructive	• Analytical
4). End Product	• F/statment	• Audit Report

Types of Audits

→ Mainly there are 4-types of Audits:-

- 1). Financial Statement Audit
- 2). Operational / Performance Audit
- 3). Compliance Audit
- 4). Forensic Audit

①. Financial Statement Audit

- Is Audit on f/stat. whether they are prepared in accordance with the criteria (GAAP, IFRS).

②. Operational Audit

- Is Auditing the Performance, Operating Procedures and methods of a company for the purpose of evaluating efficiency and effectiveness.

③. Compliance Audit

- Is a type of Audit to determine whether the auditee is following specific Rules set out by some higher authority such as: mgt, govt, BoD.

④. Forensic Audit

- Is a type of Audit for the purpose of detection of fraudulent activities

Types of Auditors

a). Independent (External) Auditors

- are certified Public Accountants that has no connection to the organization.

b). Internal Auditors

- are employee of a company that work under the control of the mgt.

Difference Between Internal and Independent Auditor

Internal

- Regular employee of the company
- Appointed by mgmt
- Not mandatory
- Act as an advisor to the mgmt
- Professional Qualification isn't necessary
- Reports to the mgmt
- Is Continuous Process

Independent

- Professional appointed by the company
- Appointed by Shareholders or govt
- Is mandatory
- Independent from mgmt
- Professional Qualification is necessary
- Reports to Shareholders
- Is Periodic Process

Characteristics of Auditing Profession

- 1). Responsibility to serve the Public
- 2). Complex Body of Knowledge
- 3). Standard of admission to the Profession
- 4). Professional Associations
- 5). Need for Public Confidence
- 6). Professional Ethics:-
 - Integrity
 - Objectivity
 - Confidentiality
 - Independence
 - Caring for others
 - Accountability
 - Due-care

International Auditing Standards

→ There are two Auditing Standards:-

- a). Generally Accepted Auditing Standard (GAAS)
- b). International Standards on Auditing (ISA's).

Advantages of International Auditing Standard

* World Wide

- Increase confidence in foreign inv't

* Consistent

- International investors comprehend statements from diff countries.

* High Quality

- International Standards encourage better quality,
 & less Political Influence.



Chapter-2

Auditor's Professional Ethics and Legal Liability

→ Ethics refers to standards or codes of ~~eth~~ moral Principle on how to act, does or thinks.

Basic Ethical Principles

- Be honest
- Have Integrity
- Keeping Promise
- Be Fair
- Care for others
- Be faithful and loyal
- Respect Others
- Be Responsible citizen
- Pursue Excellence
- Be Accountable

Ethical Dilemmas

- Dilemma means a situation where we can't choose one alternative.
- A situation in w/c welfare of one or more other individuals is affected by the results of the decision.

Steps When facing Ethical Dilemmas

1. Identify the Problem
2. Identify Possible course of action
3. Identify any constraints relating to decision
4. Analyze the likely effects of Possible course of action.
5. Select the best course of action.

Example

#. Assume your wife/husband is suffering from cancer disease and you find a cure for \$100,000 but you only have \$50,000 & then what will you do?

- Stealing money / the medicine from the Pharmacy
- Don't steal the money / medicine & you wait.

(x). The Above two alternatives have their own effects stealing (bad thing) or death of wife/husband (also bad).

Auditing Rules of Professional conduct

1). Independence

- Auditors must be Independent to avoid any biased attitude

2). Confidential client info

- Auditors shall not disclose (reveal) clients info without their consent unless for courts or other legal issues.

3). Integrity, Objectivity, Due care

- Integrity is being honest
- Objectivity is being free from bias
- Due care is applying appropriate level of care and skill

4). Competence

- Undertaking / fulfilling what the profession need.

5). Adherence to GAAS, GAAP or ISA, IFRS

6). Advertising and Solicitation

- Audit firm shall not advertize its company in a misleading / false way.

7). Contingent Fees

- Auditors shall not charge a fee contingent on the outcome of an audit or review.

8). Communication with Predecessor Auditor

- Communicate the previous Auditor before accepting an appointment.

Auditors Responsibility

- > Auditors Responsibility is to give opinion / detecting material misstatement in F/s statements.
- > Independent Auditors have the ff Responsibility :-

(1). Asses the risk that error & irregularities may cause a clients F/s to be materially misstated.

(2). Designing Audit Procedures that helps to give appropriate opinion.

Who might sue an auditor

<u>Plaintiff</u>	<u>Reason</u>	<u>Type of Liability</u>
1). Client	• For failing to discover defalcation, Inappropriate withdrawal from an audit, breaching confidentiality.	• Common Law Liability to client
2). 3 rd Party	• For failing to discover material misstatements	• Common Law Liab to the 3 rd parties
3). Group of Shareholder	• Not discovering materially misstated F/s stat.	• Common Law Liab. to the 3 rd parties
4). GOV't	• For knowingly report an incorrect audit report	• Criminal Liability.

Important Terms

- (1). Ordinary Negligence
 - Is failure to perform a duty in accordance with applicable Professional standard.
- (2). Gross Negligence
 - Is lack of even a slight care

(3). Fraud

- misinterpretation of material fact with the intent to deceive (harm) the other party.

(4). Constructive Fraud

- Same as fraud but it doesn't involve misinterpretation with the intent to deceive the other party

(5). Privity

- Is the relationship in CPA firms & clients or 3rd parties.

(6). 3rd Party Beneficiary

- A person named in the contract having rights and benefits under the contract.

(7). Engagement letter

- Is written contract summarizing the contractual relationship.

(8). Breach of contract

- Failure to perform in accordance with the contract

(9). Proximate Cause

- Exists when damage to another is directly related to the wrongdoer's act.

(10). Plaintiff

- The party that claims damage & brings suit against defendant

(11). Contributory Negligence

- Exists when the negligence is coming not from only the auditor rather by the clients also (Plaintiff).

Ex - Clients may not give sufficient evidence

(12). Comparative Negligence

- When parties both contribute to the negligence the court decides to allocate the damage between negligent parties.

When Auditors are Legally Liable

- * If the Auditor isn't doing his work Negligently (Not by due-care)
- * Or when there is a Proximate cause b/w the auditors negligence and the damage (loss) of the Plaintiff (suing party).

~~Therefore~~ Not detecting frauds / embezzlement activities is not sufficient to make the auditors liable b/c detecting this kind of activities is mgmt's role, besides auditors take sample while conducting their work so it is impossible to assess each and every txns of a co.'s F/S.

Legal Concepts Applied To Auditors Liability

(1). The Prudent Person concept

- > An Auditor ability to care (due-care)

(2). Liability For the Acts of others

- > You are liable for your Partners, employees etc

(3). Lock of Prerogative Communication

- > We said that in any case an auditor must not reveal clients info. but in some cases it should reveal.
Eg - When court orders

(4). Negligence

- > Absence of reasonable care, Therefore the Plaintiff must Prove the ff:-

- * Defendant owed duty of care
- * Defendant was Negligent
- * Plaintiff suffered a loss
- * There is direct R/ship b/w Defendant's negligence & the Plaintiff's loss.

(5). Tort Action For Negligence

- > Failure to meet social / Professional obligation w/c cause an injury to another person.

(6). Fraud

- > Intentional / knowingly / recklessly doing false activity

(7). Constructive Fraud

- > A fraud w/c is unintentional / with no intent for harm

(8). Breach of Contract

- > Failure to perform in accordance with the contract.

(9). Common Law

- > Laws that have been passed by court decision
Eg. - Jury

(10). Statutory Law

- > Laws that have been passed by the Gov't

(11). Contributory Negligence

- > When the clients also contribute to the loss.

Auditors Defence Against Clients Suit

(a). Lack of Duty

- > It means it is not mentioned in the contract

(b). Absence of Negligence

- > It means the Auditor perform this work with due care and in accordance with GAAS / ISA.

(c). Contributory Negligence

- > It means the client is also contributed to the loss (damage) occurred.

(d). Absence of casual connection

- > It means there is no connection b/n Auditors negligence and the loss occurred.

Measures To Reduce Auditors Exposure To Lawsuits

a. Professional Measures

- Encouraging Auditing Researches
- Establishing Standards / Rules
- Establish Requirement that Protect auditors
- Establish Practice inspection Requirements
- Oppose Unwarranted Lawsuits
- Educate FIs users about auditing & auditors opinions
- Sanction Auditors for Improper Conduct.

b. Individual Measures

- Deal Only with Clients having Integrity
- Hire, Train and Supervise Qualified Personnel
- Follow Professional standards
- Maintain Independence
- Understand Clients business
- Perform Quality audits
- Obtain Engagement letter & representation letter

Audit Planning and Analytical Procedures

- > Audit Planning is thinking in Advance before Auditing Performed.
- > Field Work Standard say its mandatory to Plan

Types of Audit Planning

- a). Pre-Engagement Plan - Whether to Accept or Reject a client
- b). Engagement Planning - About specific steps that help determining an overall Audit Strategy.

Reasons for Planning

- (1). To Obtain Sufficient Competent Info
 - To minimize Legal Liability and if Internal control is weak no evidence to obtain increases
- (2). To help keep audit cost reasonable
 - If weak Internal control need high amount of evidence to obtain and this ↑ the audit cost
 - ↑ cost may not attract customers
- (3). To Avoid misunderstanding with client
 - For good Relsnshp

Risks To Consider in Audit Planning

- a). Acceptable Audit Risk
 - The risk that you are willing to accept on w/c f/stat. may be materially misstated & go for unqualified opinion.
Eg - sampling error
- b). Inherent Risk
 - The risk of material misstatement in account balance before considering Internal control.
Eg - Auditor may conclude there is material misstatement in A/R, INV, or cash . . . etc.

Steps in Audit Planning

→ There are 7-steps in audit Planning.

#1. Accepting client and Performing Initial Audit Planning

→ It involves 4-things:-

(a). Client Acceptance and Continuance

- Whether to accept old client or new client
- If Audit firms accept risky client they ask higher fees.

(b). Identify Clients Reason for Audit

- For Debt Purpose, Tax Purpose, or for many user (PLC, corpora)

(c). Obtaining An Understanding With Client

- To Avoid conflict an engagement letter is mandatory.

(d). Selecting staff for Engagement

- The Audit is to be Performed by a Person having adequate training and Proficiency as an auditor.

#2. Understand Client's Business and Industry

→ It is a thorough understanding about clients business, Industry and knowledge about their operation.

#3. Assess Client's Business Risk

→ Client's Business Risk may cause material misstatement so the auditors Primary concern is to assess material misstatement in F/Stat. due to the business risk.

#4. Set materiality and Assess Acceptable Audit risk and Inherent Risk

#5. Preliminary Analytical Procedures

- > Involves Computations of Ratios and other Component of recorded amount.
- > Used in Planning to Understand Clients Business & Industry.
- > Used to Identify misstatements, Reduces detailed tests and assess going concern issue.

Purpose

	<u>Planning</u>	<u>Testing</u>	<u>Completion</u>
• Understand client's BUs. and Industry	• Primary Purpose	• Non	• Non
• Assess going concern	• secondary >>	• Non	• secondary >>
• Indicate misstatement	• Primary >>	• secondary >>	• Primary >>
• Reduces detail test	• Secondary >>	• Primary >>	• Non

Types of Analytical Procedures

- *. Compare client and Industry data
- *. Compare client data with Prior Period data
- *. Compare client data with client-determined expected results
- *. Compare client data with Auditor-determined expected results
- *. Compare client data with Expected result using non-fin. data

#6. Understand Internal Control & Assess Control Risk

- > Control Risk is the risk that material misstatement Presented or detected by internal control.
- > Then Auditor Evaluates Effectiveness of Internal control to Prevent material misstatement and Prepare Preliminary assessment of Control Risk.

#7

Develop Overall Audit Plan and Audit Program

→ Involves decision about the nature, extent and timing of audit tests.

Types of Tests

- In developing overall audit plan auditors have 5-Types of tests:-
 1. Procedures to obtain an understanding of Internal control
 2. Tests of control
 3. Substantive Tests of Trn
 4. Analytical Procedures
 5. Tests detailed Balances.
- Then the auditor select w/c type of tests to Perform b/c its costly to asses all type of tests.

Chapter - 4

Internal Control (IC)

- > IC is Policies and Procedures for safeguarding the company's Asset and Liabilities
- > IC is checks and Balances of orderly and efficient conduct of business.

Why Auditor must Understand IC

(1). It Tells the Auditor to Plan

EG - If the IC is weak the time and evidence will ↑, and we have to Plan

(2). To Assess Audit Risk / Control Risk

Key Concepts of IC

- IC is Responsibility of a Client (mgt)
- IC Provide ONLY Reasonable Assurance not Absolute
- IC has Inherent limitation that can't be avoided
- IC is a Process not an end by itself
- IC affected by Peoples

Types of IC

(#1). Detective Control

- > Designed to detect error that occurred already

EG - Physical Inventory, Checking trans

(#2). Preventive Control

- > Designed to keep errors from occurring

EG - Separation of duties, Adequate Documentation

Responsible Parties for IC

* Board of Directors

* Senior mgt

* Financial mgt

* Internal Auditor staff

* Independent Auditor - BUT for only giving opinion in deficiency of IC

Elements of IC

→ are 5-Elements:-

1. Control Env't
2. Control Activities
3. Risk Assessment
4. Info. and Communication
5. Monitoring

(*)

Control Env't

→ Is the perceived attitude of clients mgt about IC

Factors Related To Control Env't

• There are 9-factors

(a). mgt Philosophy and Operating style

→ Intems off the ff:-

- * Business Risk
 - Risk Taker
 - Risk Aversor
- * Attitude towards financial Reporting
- * Attitude towards Achieving goal

(b). Effectiveness of BOD and Audit Committee

→ Communication Bn BOD, Internal and External Auditors

→ The factors for effectiveness are:-

- * Audit committees Independence from mgt
- * Experience
- * Interaction with each other.

(c). Organizational Structure

- Tall Structure and flat structure
- Well structured orga has separation of responsibilities, then it will have better IC.

(d). Assignment of Authority and Responsibility

- Clear understanding of responsibility within employees.

(e). System Dev't methodology

- Does mgt have methodology for developing and modifying system?

(f). Personel Policies and Practices

- The mgt should ensure that Competent, trustworthy & motivated Personnel are employed to meet Client's goal & objectives.
- Even Poorly designed system may be effective if there are good Personnel.

(g). mgt's Reaction to External Influence

- for dlt changes like Economical, Technological . . . etc

(h). Internal Audit

- Does Internal Audit exist?
- If exists, does it assist External Auditor - b/c it does Audit fee.

(i). Integrity and Ethical Values

- Those who create, administer and monitor controls should have Integrity and Ethical Values.

#2

Control Activities

- > Policies, Procedures and directives takes to achieve objectives.

Key Factors

(a). Adequate segregation of duty

- It Reduces Fraud

ES - segregating the one that authorizes check

(b). Proper Authorization of Trans and Activities

i. General Authorization - the general Policy

ES - Policy on sales, A/R . . . etc

ii. Specific Authorization - Authorization case by case

ES - seeing how Pdt x is Run or sold

(c). Adequate document and Record

- For Trns to be correctly recorded there must be adequate document. EG - Re numbering.

(d). Adequate safeguard over Asset and Record

- Locking room, fencing areas, fire proof, security guard, Backup....

(e). Independent check on Performance

- Reviewing Performance by Independent of those Performing work.

#3. Risk Assessment

- > The Process Used to Identify, analyze and manage relevant risk w/c may affect entity's objective.

Key Factors

- | | |
|---------------------------------|-------------------------------|
| (a). Changes in Operating Env't | (e). New Technology |
| (b). New Personnel | (f). Accounting Pronouncement |
| (c). New Info system | (g). Foreign operations |
| (d). Rapid growth | |

#4. Info. and Communication system

- > method to initiate, record, Process and report trns

Info to be communicated

- | | |
|-----------------|--------------------|
| • Org's Plan | • Control Activity |
| • Control Env't | • Performance |

Direction of Commu

- Upward - from employee to top manager
- Downward - from mgr to employee
- Across - within the same status employees

Info system

- * Formal
- * Informal

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monitoring

- > Is Evaluating Performance
- > Are two types:-

(a). Ongoing Monitoring

- Regularly Performed Supervisory and mgt activities

(b). Separate (Periodic) Evaluation

- Performed on non-routine basis

Ex- Periodic Audit by Internal Auditors

Why monitoring: to determine whether

- * IC is operating as intended
- * Any modifications are necessary

Method of studying IC

- Review Prior Year Working Paper
- Interview Prior Year auditor, Client's Personnel
- Study Client Policies and Procedure
- Study Client's Document, Record, Info and comm. sys.

Method of documenting the understanding IC

1. Narratives

- > Through Writings

2. Flow Chart

- > Diagram

3. IC Questionnaires

- > Series of Question

Advantage of IC Questionnaire

- * Can cover most aspect of IC
- * Can be quickly reviewed for weakness

Disadvantage of IC Questionnaire

- * The Questionnaire may be vast
- * Reliability Problem

• Following are descriptions of ten internal controls.

1. The company's computer systems track individual transactions and automatically accumulate transactions to create a trial balance.
2. The company must receive university transcripts documenting all college degrees earned before an individual can begin their first day of employment with the company.
3. Senior management obtains data about external events that might affect the entity and evaluates the impact of that information on its existing accounting processes.
4. Each quarter, department managers are required to perform a self-assessment of the department's compliance with company policies. Reports summarizing the results are to be submitted to the senior executive overseeing that department.
5. Before a cash disbursement can be processed, all payee information must be verified by matching the payee to the company's approved vendor listing.
6. The system automatically reconciles the detailed accounts receivable subsidiary ledger to the accounts receivable general ledger account on daily basis.
7. The company has developed a detailed series of accounting policy and procedures manuals to help provide detailed instructions to employees about how controls are to be performed.

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8. The company has an organizational chart that establishes the formal lines of reporting and authorization protocols.
9. The compensation committee reviews compensation plans for senior executives to determine if those plans create unintended pressures that might lead to distorted financial statements.
10. On a monthly basis, department heads review a budget to actual performance report and investigate unusual differences.

Indicate which of the five COSO internal control components is best represented by each internal control.

- | | |
|------------------------|----------------------------------|
| a. Control environment | d. Information and communication |
| b. Risk assessment | e. Monitoring |
| c. Control activities | |

- `solution
- 1. Information and communication
- 2. Control environment
- 3. Risk assessment
- 4. Monitoring
- 5. Control activities
- 6. Information and communication
- 7. Control activities
- 8. Control environment
- 9. Risk assessment
- 10. Control activities

Chapter-5

Audit Evidence and Documentation

mgmt Assertion

-> Is claim or Representation of the mgmt in the F/statements

-> On F/stat. There are 5-mgmt Assertions:-

(1). Assertion About Existence or occurrence

- The Asset, Liability, O.E, Rev. and Exp are actually occurred | exists

(2). Assertion About Completeness

- All Trans are Included in the F/statements

(3). Assertion About Rights and Obligation

- The Asset are the rights of client and
- The Liability are the obligations of the client

(4). Assertion About Valuation | Allocation

- Determination of Value of Asset, Liab., O.E, Rev. and Exp are determined according to GAAP | IFRS

(5). Assertion About Presentation and Disclosure

- The Accounts in the F/statment are Prepared in accordance with GAAP | IFRS.

Audit Objectives

(a). Trxn Related

(b) Balance Related

(a). Trxn Related

- It is related to trxn
- There are 6 - trxn related objectives

- * Existence is recorded then really exist
- * Completeness does all trans are recorded
- * Accuracy does recorded trans are stated correctly
- * Classification is there Proper Classification in Journal and ledger
- * Timing Is trans recorded at correct date
- * Posting and summarization Trans are Properly Posted and Summarized in the master file (ledger).

(b) Balance - Related

- It is related to Balance (sum)
- There are 9 - Balance related objectives:-
 - * Existence
 - * Completeness
 - * Accuracy
 - * Classification
 - * Cutoff Trans near the B/sheet date are recorded in Proper Period. Ex - Accrual base
 - * Detail-Tie the bal. in Journal & ledger must be equal
 - * Realizable Value Assets are included at the amount estimated to be realized.
 - * Rights and Obligation Assets are right and Liab. one oblign
 - * Presentation & Disclosure the balance and related disclosure requirements are Properly Presented in F/s statements.

Audit Evidence

- In order to give opinion auditors must gather Audit evidences
- It is any evidences that are collected and used by the auditor to give his/her opinion.
- It must be competent and sufficient

Competent

- Is about quality and reliability
- When quality of evidence $\rightarrow$ the no of evidence to be collected $\downarrow$ or

Sufficiency

- Is about quantity | No | Volume
- Determined by judgement

-> Reliability of Audit Evidence is affected by:-

1. Source

- * Evidence from Auditor: Exceptionally reliable
- * Evidence from 3rd Party: reliable
- * Evidence from mgmt / client: least reliable

2. IC

- * Strong IC has high competency & vice versa.

Types of Audit Evidence

-> There are 7-types of Audit Evidence

#1

Physical Examination | Evidence

- Obtained from Physical Examination or Inspection of Asset
Eg- Inv. counting
- Gives direct knowledge to the Auditor, but not all assets in the company is their own.

#2

Confirmation

- Describes the receipt of written or oral response from independent 3rd Party verifying accuracy of info. requested
- 1st Client sent letter to 3rd Party and then 3rd Party directly respond to the auditor.
- It is costly & as much as possible it must be written.

i. Positive Confirm

* asking 3rd party / recipient to respond in all circumstances

ii. Negative Confirm

* asking in only when info are incorrect

#3. Documentary Evidence

- Includes check, Invoice, Contract --- etc obtained from client
- It may be:- Generated from ext. or Int.

i. External like Purchase

ii. Internal like sales

* When Auditor use documentation to support recorded transaction it is called Vouching

* When Auditor Traces from receiving report to acquisition Journal to satisfy completeness it is called Tracing.

#4. Analytical Evidence

- Is comparisons and r/ships to assess whether account bal. appear reasonable
- Used to check reliability of evidence
- help to understand clients strength and weakness

Uses to

- * Understand clients Industry and Business
- * Assess the entity's ability as going concern
- * Indicate possible misstatement in F/statement
- * Reduce detailed Audit tests

#5. Inquiries of the client

- Is obtaining of written or oral info from client
 - It is not conclusive b/c it may be biased or not Independent.
- ES - Seeing IC before audit work

#6. RePerformance

- Is rechecking a sample of computations and Transfers of info made by client
- Is done by computer softwares

#7. Observation

- Is the use of the senses to asses certain activities
- ES - Auditor may tour the Plant offices.

Level of Reliability

- High
- medium
- Low

Type of Evidence

- Phy- Exams and RePerformance
- Docums, Confirms & Analytical
- Inquiries, and Observation

Audit Documentation

- > Is the records kept by the auditor's Procedures, tests info and conclusions.
- > Also called Working Paper

Purposes of Audit Documentation

- To aid the auditor in providing reasonable assurance
- A Basis for Planning the audit
- A Record of the evidence accumulated and results of test
- Data for determining proper type of Audit report
- A Basis for review by supervisors & Partners

Confidentiality of Audit files

- * The Auditor must not divulge info to outsiders at any time

Content and Orgn of Audit files

- > Permanent file contain historical data or continuing nature
 - Include
 - Copies of article of incorporation, bond indenture, contract
 - Long term debt, D.E, Fixed asset - - - etc
 - Orginal Chart, Flow Chart, Resonarie, other IC Info
 - Ratio's and Percentages of Previous Year audit.
- > Current file contain audit documentation applicable to the current year under audit
 - Include
 - Audit Program / Procedure
 - General Info like Audit Planning memos, BAP meetings, etc
 - Working trial Bal.
 - Adjusting and reclassification Entries
 - Supporting Schedules

Ratio's of Audit Documentation

- * Each Audit file should be properly Identified
- * Audit documentation should be Indexed and cross referenced
- * Completed audit docs must clearly indicate audit work performed.
- * Audit documentation should include sufficient info to meet the obj.
- * The conclusion reached should be stated.

Chapter-6

Audit Report

- > Audit Report is the final step of the audit process
- > The Type of F/S you require to give audit report are:-
 - Balance Sheet
 - Income Statement
 - Statement of Retained Earnings (A-E)
 - Statement of Cash flow
 - Notes to F/S statement

Components of Audit Report

- * Report Title - Independent Auditor Report
- * Address - to the company, Shareholders, BOD
- * Introductory Paragraph
- * Scope Paragraph
- * Opinion Paragraph
- * Name of Audit firm and signature
- * Date of Audit Report

Introductory Paragraph

- It makes simple statement that the audit firm has done an audit.
- It lists Type of F/S statements audited
- It also states F/S statements reports of mgt and expressing opinion is auditors report.

Scope Paragraph

- Describes what the auditor has performed during the audit
- States whether the audit was performed according to ISA or GAAs and describes the audit is designed to give reasonable assurance.

Opinion Paragraph

- Contains the auditors opinion on whether the F/S statement are prepared according to ISA/GAAs.

Types of opinion

#1

Unqualified opinion - Standard Report

- States a clean opinion with no significant scope limitation
- Required condition for these report are:-

* The F/S are Prepared in accordance with ISA/GAAS
* The Auditor was performed >> >> >>.

#2

Unqualified opinion - with explanatory language

- Some times explanatory language may be added in unqualified opinion.

#3

Qualified opinion

- States that F/S are presented fairly in accordance with GAAP/IFRS except in some areas

#4

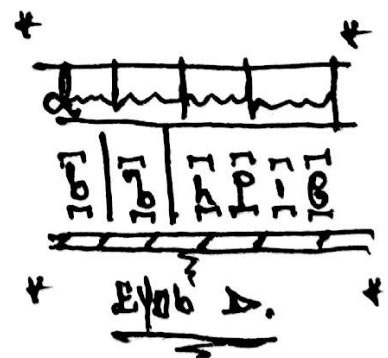
Adverse opinion

- States that F/S aren't presented fairly in accordance with IFRS/GAAP.

#5

Disclaimer opinion

- States that due to scope limitation the auditors were unable to reach into conclusion.
- There is no sufficient document | evidence in the 1st place.



Modifications of the Auditors' Report-- Unqualified Opinions

Type of Report	Introductory or Scope paragraph	Explanatory Paragraph	Opinion Paragraph
Shared responsibility	Describe work of other auditors	None	"...based on our audit and the report of other auditors"
Going concern uncertainty	None	Describe uncertainty	None
GAAP not consistent	None	Describe change in principle	None
Emphasis of a matter	None	Describe matter	None
Justified departure from GAAP	None	Describe departure	None

Modifications of Auditors' Report—Qualified Opinions

Type of Report	Introductory or Scope Paragraph	Explanatory Paragraph	Opinion Paragraph
Qualified—GAAP Departure	None	Describe departure and effects	“except for the effects of the departure the financial statements...”
Qualified—Scope Limitation	“Except as explained in the following paragraph...”	Describe scope limitation	“except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to...”

Modifications of Auditors' Report—Adverse Opinions and Disclaimers

Type of Report	Introductory or Scope Paragraph	Explanatory Paragraph	Opinion Paragraph
Adverse	None	Describe reason for opinion	"The financial statements do not present fairly"
Disclaimer of Opinion--Scope Limitation	"We were engaged"; Omit responsibility. Omit scope paragraph	Describe scope restriction and any reservations	"we do not express an opinion on the financial statements."