

Audit and Assurance Cheat Sheet

Introduction to Assurance

Definition: An assurance engagement is one where a **practitioner** obtains sufficient appropriate evidence to express a **conclusion** designed to enhance the **intended users'** confidence about a subject matter against specific criteria.

Five Elements of Assurance:

1. **Three-party involvement:** The practitioner (reviewer), intended users (decision-makers), and the responsible party (preparers of the information).
2. **Subject matter:** The data or information under examination.
3. **Suitable criteria:** The standards or laws used to evaluate the subject matter (e.g., IFRS).
4. **Sufficient appropriate evidence:** The quantity and quality of data needed to support the conclusion.
5. **Written assurance report:** The final output containing the practitioner's opinion.

Levels of Assurance:

- **Reasonable Assurance:** Provides a **high level** of confidence through a **positive** opinion (e.g., "In our opinion, the financial statements give a true and fair view"). **External audits** are a primary example.
- **Limited Assurance:** Provides a **moderate level** of confidence through a **negative** conclusion (e.g., "Nothing has come to our attention that causes us to believe..."). **Review engagements** typically provide limited assurance.

True and Fair: "True" means information is factually correct and conforms to standards; "Fair" means it is clear, impartial, and reflects commercial substance.

Expectation Gap: This refers to public **misconceptions** about the auditor's role, such as the belief that auditors test every transaction or provide a 100% guarantee of accuracy

Rules and Regulation

Need for Regulation: High-profile audit failures, such as **Enron**, led to initiatives focusing on audit quality, harmonisation of procedures, and strict ethical codes.

Auditor Eligibility: To act as an auditor, an individual must be a member of a **Recognised Supervisory Body (RSB)**, such as the ACCA, or be directly authorised by the state.

Exclusions: Those who manage, work for, or have close business/personal connections with a company are legally excluded from auditing it.

Auditor Rights: During their appointment, auditors have the right to **access all books and records**, receive necessary information and explanations, and **attend any general meeting** of the company.

Appointment and Removal:

- **Appointment:** Usually performed by the **shareholders** (members) through voting.
- **Removal:** Achieved by a **simple majority** at a general meeting; the auditor has the right to circulate representations explaining why they should not be removed.
- **Resignation:** An auditor may resign by providing written notice and a **statement of circumstances** to the members and regulatory authorities.

Regulatory Bodies:

- **IFAC:** The global organisation for the accountancy profession.
- **IAASB:** A subsidiary of IFAC that develops **International Standards on Auditing (ISAs)**.
- **FRC:** The UK regulator responsible for overseeing the profession and modifying ISAs for national use

Ethics and Acceptance

Conceptual Framework: Auditors follow a principles-based approach to identify **threats** to fundamental principles and apply **safeguards** to reduce them to an acceptable level.

Fundamental Principles:

1. **Integrity:** Being straightforward and honest.
 2. **Objectivity:** Avoiding bias, conflict of interest, or undue influence.
 3. **Professional Competence and Due Care:** Maintaining knowledge and acting diligently.
 4. **Confidentiality:** Not disclosing client information without proper authority.
 5. **Professional Behaviour:** Complying with laws and avoiding discrediting the profession.
- **Five Categories of Ethical Threats:**
 1. **Self-interest:** Financial or other interests (e.g., owning shares, fee dependency).
 2. **Self-review:** Auditing one's own work (e.g., preparing the financial statements being audited).
 3. **Advocacy:** Promoting a client's position (e.g., representing them in a legal dispute).
 4. **Familiarity:** Being too sympathetic due to close relationships or long association.
 5. **Intimidation:** Actual or perceived pressure from the client.

Confidentiality Exceptions: Disclosure is permitted if **required by law, permitted by law and authorised by the client**, or if there is a **professional duty/right** to disclose (e.g., to the ACCA).

Acceptance Procedures:

- **Professional Clearance:** Asking the client for permission to contact the **outgoing auditor** for any relevant information.
- **Preconditions for an Audit:** Management must acknowledge their responsibility for **preparing financial statements**, maintaining **internal controls**, and providing **access to information**.

Risk

Audit Risk Definition: This is the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated. It comprises the **risk of material misstatement** and **detection risk**.

Risk of Material Misstatement (RMM): This is the risk that financial statements are misstated prior to the audit and is composed of **inherent risk** and **control risk**.

- **Inherent Risk:** The susceptibility of an assertion to a material misstatement before considering any related controls. Factors include complexity, subjectivity, change, and uncertainty.
- **Control Risk:** The risk that a material misstatement will not be prevented, or detected and corrected, on a timely basis by the entity's internal controls.

Detection Risk: The risk that the auditor's procedures will not detect a material misstatement. It includes **sampling risk** (the sample is not representative) and **non-sampling risk** (inappropriate procedures or failure to recognise a misstatement).

Materiality: Information is material if omitting, misstating, or obscuring it could reasonably be expected to influence the economic decisions of users.

- **Performance Materiality:** A lower amount set to reduce the probability that the aggregate of uncorrected/undetected misstatements exceeds overall materiality.

Professional Scepticism: An attitude involving a questioning mind, being alert to conditions indicating possible fraud or error, and a critical assessment of audit evidence.

<ul style="list-style-type: none"> ○ Engagement Letter: A contract sent before the audit to confirm acceptance and set out the objective, scope, and responsibilities of both parties 	
<p style="text-align: center;">Planning</p> <ul style="list-style-type: none"> • Purpose of Planning: The objective is to plan the audit so it is performed in an effective and efficient manner. • Benefits: It helps the auditor devote attention to important areas, identify potential problems timely, and properly organize the team. • Audit Strategy: Sets the scope, timing, and direction of the audit. It guides the development of the audit plan and determines the resources to be deployed. • Audit Plan: A more detailed document that describes the nature, timing, and extent of risk assessment procedures and further audit procedures. • Interim vs. Final Audit: <ul style="list-style-type: none"> ○ Interim Audit: Performed before the year-end to document systems, evaluate controls, and test transactions for the year to date. ○ Final Audit: Takes place after the year-end to obtain evidence for the final auditor's report, focusing on year-end balances and financial statement review. • Audit Documentation: Auditors must prepare written documentation that provides a basis for their report and evidence that the audit was performed in accordance with International Standards on Auditing (ISAs). 	<p style="text-align: center;">Evidence</p> <ul style="list-style-type: none"> • Audit Evidence Objective: Auditors must design procedures to obtain sufficient appropriate evidence to draw reasonable conclusions for the audit opinion. • Sufficiency vs. Appropriateness: <ul style="list-style-type: none"> ○ Sufficiency is the measure of the quantity of evidence. ○ Appropriateness is the measure of quality, involving relevance and reliability. • Reliability Principles: Evidence is more reliable when obtained from independent external sources, obtained directly by the auditor, or exists in original documentary form. • Financial Statement Assertions: <ul style="list-style-type: none"> ○ Transactions/Events: Occurrence, Completeness, Accuracy, Cut-off, Classification, Presentation. ○ Account Balances: Existence, Rights and Obligations, Completeness, Accuracy/Valuation/Allocation, Classification, Presentation. • Types of Procedures: These include Inspection (records or assets), Observation (witnessing a process), External Confirmation (third-party response), Recalculation (mathematical accuracy), Reperformance (executing client controls), Analytical Procedures (evaluating relationships), and Enquiry. • Audit Sampling: The application of procedures to less than 100% of items within a population so that all sampling units have a chance of selection.
<p style="text-align: center;">Systems and Controls</p> <ul style="list-style-type: none"> • Five Components of Internal Control: <ol style="list-style-type: none"> 1. Control Environment: The "tone at the top," including management's integrity and ethical values. 2. Entity's Risk Assessment Process: How management identifies and addresses business risks relevant to financial reporting. 3. The Information System and Communication: Procedures designed to initiate, record, and report transactions. 4. Control Activities: Policies and procedures to achieve control objectives (e.g., Authorisation, Reconciliations, Physical controls). 5. Monitoring: Continual evaluation of control effectiveness. • Control Activities Examples: <ul style="list-style-type: none"> ○ Authorisation: Signing a purchase order to ensure validity. ○ Segregation of Duties: Splitting responsibilities to reduce fraud risk. ○ Physical Controls: Locked safes or password restrictions. • IT Controls: Divided into General Controls (e.g., access, program changes) and Information Processing Controls (e.g., batch totals, sequence checks). • Tests of Controls: Audit procedures designed to evaluate the operating effectiveness of controls in preventing or detecting material misstatements. • Reporting Deficiencies: Auditors must communicate significant deficiencies in writing to those charged with governance. 	<p style="text-align: center;">Internal Audit</p> <ul style="list-style-type: none"> • Definition: Internal audit is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. • Need for Internal Audit: Factors include the scale and diversity of activities, complexity of operations, number of employees, and the results of a cost/benefit analysis. • External vs. Internal Audit: <ul style="list-style-type: none"> ○ Objective: External audit expresses an opinion on the truth and fairness of financial statements; internal audit reviews the efficiency and effectiveness of internal controls. ○ Reporting: External auditors report to shareholders; internal auditors report to management or those charged with governance. ○ Scope: External audit focuses on the financial statements; internal audit is wide in scope and determined by management's requirements. • Internal Audit Assignments: <ul style="list-style-type: none"> ○ Value for Money (VFM): Focuses on the three Es: Economy (least resources), Efficiency (outputs vs. inputs), and Effectiveness (achieving objectives). ○ Other Roles: These include investigating fraud, monitoring compliance with laws, performing operational audits to streamline processes, and auditing IT systems. • Outsourcing: <ul style="list-style-type: none"> ○ Advantages: Access to specialist expertise, greater independence from internal management, and flexibility in employment costs. ○ Disadvantages: Lack of intimate organizational knowledge, potential for high fees, and ethical threats if the external auditor provides the service.
<p style="text-align: center;">Procedures</p> <ul style="list-style-type: none"> • Writing Good Procedures: Every procedure should contain an action (e.g., inspect), a source (e.g., purchase invoice), and an objective (e.g., to verify existence). • Directional Testing: 	<p style="text-align: center;">Completion and Review</p> <ul style="list-style-type: none"> • Subsequent Events (ISA 560): Events between the reporting date and the date the auditor's report is signed.

<ul style="list-style-type: none"> ○ Understatement (Completeness): Sample from outside the system (e.g., goods received notes) and trace into the accounting records. ○ Overstatement (Existence/Occurrence): Sample from the accounting records (e.g., sales day book) and trace back to supporting documentation. ● Procedures for Specific Items: <ul style="list-style-type: none"> ○ Bank and Cash: Assertions are existence and valuation; procedures include bank confirmation letters, reviewing bank reconciliations, and performing cash counts. ○ Non-Current Assets: Procedures include physical inspection (existence), inspecting title deeds (rights and obligations), and recalculating depreciation (valuation). ○ Inventory: Attendance at the inventory count is vital to observe performance and perform test counts; final records are tested for cut-off and NRV. ○ Receivables: The primary procedure is a receivables circularisation (direct confirmation) to verify existence; after-date cash receipts verify valuation. ○ Payables: Focus is on completeness; procedures include supplier statement reconciliations and reviewing post-year-end invoices for unrecorded liabilities. 	<ul style="list-style-type: none"> ○ Adjusting Events: Provide evidence of conditions existing at the reporting date (e.g., bankruptcy of a customer); require adjustment of figures. ○ Non-Adjusting Events: Relate to conditions arising after the reporting date (e.g., a fire); require disclosure if material. ● Going Concern (ISA 570): The assumption that the entity will continue for at least 12 months from the reporting date. <ul style="list-style-type: none"> ○ Responsibilities: Directors must assess ability to continue; auditors must obtain sufficient appropriate evidence to conclude on this assessment. ○ Indicators: Net current liabilities, defaulted loans, loss of key staff, or emergence of successful competitors. ● Written Representations (ISA 580): Written statements by management to confirm certain matters or support other audit evidence. They are not a substitute for more reliable evidence. ● Overall Review: Auditors must ensure the financial statements comply with accounting standards and that analytical procedures corroborate their conclusions. ● Evaluation of Misstatements: Auditors must accumulate all misstatements (except trivial ones) and request management to correct them; uncorrected misstatements must be assessed for materiality in aggregate.
<p style="text-align: center;">Reporting</p> <ul style="list-style-type: none"> ● Audit Opinion Types: <ul style="list-style-type: none"> ○ Unmodified: Used when financial statements are prepared, in all material respects, in accordance with the reporting framework. ○ Qualified: "Except for"—used when misstatements or lack of evidence are material but not pervasive. ○ Adverse: Used when misstatements are both material and pervasive (the statements do not give a true and fair view). ○ Disclaimer: Used when the auditor cannot obtain evidence and the effects could be both material and pervasive (the auditor does not express an opinion). ● Standard Report Sections: <ul style="list-style-type: none"> ○ Opinion & Basis for Opinion: States the conclusion and refers to professional standards followed. ○ Key Audit Matters (KAM): For listed companies; describes matters of most significance in the current audit. ○ Material Uncertainty Related to Going Concern: Included if a material uncertainty is adequately disclosed in the financial statements. ○ Emphasis of Matter: Used to draw attention to a matter already appropriately disclosed in the financial statements that is fundamental to user understanding. ○ Other Matter: Communicates matters not disclosed in the financial statements that are relevant to understanding the audit or the report. ● Reporting Misstatements in Other Information (ISA 720): If an uncorrected material inconsistency exists in the annual report (e.g., Chairman's statement), it must be described in the Other Information section. 	