AUDITING

ACCOUNTING TECHNICIAN DIPLOMA

ATD LEVEL III

STUDY TEXT
CONTENT

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   - Explain the principles and processes of an audit
   - Differences between auditing and accounting
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TOPIC 1

NATURE, PURPOSE AND SCOPE OF AUDITING

DEFINITION OF AUDITING, AUDITOR AND AN AUDIT

Auditing

The Institute of Certified Public Accountants of Kenya (ICPAK) defines auditing as the independent examination of and expression of opinion on, the financial statements of an enterprise by an appointed auditor in pursuance of that appointment and in compliance with any relevant statutory obligation,

Auditing the independent examination of and expression of opinion on, the financial statements of an enterprise by an appointed auditor in pursuance of that appointment and in compliance with any relevant statutory obligation

Auditor

"Auditor" is used to refer to the person or persons conducting the audit, usually the engagement partner or other members of the engagement team, or, as applicable, the firm. Where an ISA expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term "engagement partner" rather than "auditor" is used. "Engagement partner" and "firm" are to be read as referring to their public sector equivalents where relevant.

An official whose job it is to carefully check the accuracy of business records. An auditor can be either an independent auditor unaffiliated with the company being audited or a captive auditor, and some are elected public officials. The term is sometimes synonymous with "comptroller." Auditors are used to ensure that organizations are maintaining accurate and honest financial records and statements

Audit

This is the independent investigation into the quality of published accounting information.

An audit is the independent examination of and expression of an opinion on the financial statements of an economic entity by appointed auditor in pursuance of that appointment and in compliance with any relevant statutory obligation.

The objective of an audit is to enable the auditor express an opinion whether financial statements show a true and fair view of the company state of affairs in accordance with an identified financial reporting framework.
The purpose of an audit is not to provide additional information but rather it is intended to provide the users of the accounts with assurance that the information provided to them by directors is reliable. However, the users should not assume the auditor's opinion is one to efficiency with which management has conducted the affairs of the entity.

CONDUCT OF AN AUDIT

Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (LAS 200)

The objective of an audit of financial statements is to enable the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework.

- This International Standard on Auditing (ISA200) deals with the independent auditor's overall responsibilities when conducting an audit of financial statements in accordance with ISAs. Specifically, it sets out the overall objectives of the independent auditor, and explains the nature and scope of an audit designed to enable the independent auditor to meet those objectives. It also explains the scope, authority and structure of the ISAs, and includes requirements establishing the general responsibilities of the independent auditor applicable in all audits, including the obligation to comply with the ISAs. The independent auditor is referred to as "the auditor" hereafter.

- ISAs are written in the context of an audit of financial statements by an auditor. They are to be adapted as necessary in the circumstances when applied to audits of other historical financial information. ISAs do not address the responsibilities of the auditor that may exist in legislation, regulation or otherwise in connection with, for example, the offering of securities to the public. Such responsibilities may differ from those established in the ISAs. Accordingly, while the auditor may find aspects of the ISAs helpful in such circumstances, it is the responsibility of the auditor to ensure compliance with all relevant legal, regulatory or professional obligations.
Scope of the Audit

The auditor's opinion on the financial statements deals with whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework. Such an opinion is common to all audits of financial statements.

- The auditor's opinion therefore does not assure, for example, the future viability of the entity nor the efficiency or effectiveness with which management has conducted the affairs of the entity. In some jurisdictions, however, applicable law or regulation may require auditors to provide opinions on other specific matters, such as the effectiveness of internal control, or the consistency of a separate management report with the financial statements.
- While the ISAs include requirements and guidance in relation to such matters to the extent that they are relevant to forming an opinion on the financial statements, the auditor would be required to undertake further work if the auditor had additional responsibilities to provide such opinions.

An Audit of Financial Statements

The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. In the case of most general purpose frameworks, that opinion is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view in accordance with the framework. An audit conducted in accordance with ISAs and relevant ethical requirements enables the auditor to form that opinion.

The financial statements subject to audit are those of the entity, prepared by management of The entity with oversight from those charged with governance. ISAs do not impose responsibilities on management or those charged with governance and do not override laws and regulations that govern their responsibilities. However, an audit in accordance with ISAs is conducted on the premise that management and, where appropriate, those charged with governance have acknowledged certain responsibilities that are fundamental to the conduct of the audit. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities:

As the basis for the auditor's opinion, ISAs require the auditor to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. Reasonable assurance is a high level of assurance. It is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (that is, the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level. However, reasonable assurance is not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive.
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TOPIC 2

PLANNING FOR THE AUDIT

INTRODUCTION

An Audit plan is the specific guideline to be followed when conducting an audit. It helps the auditor obtain sufficient appropriate evidence for the circumstances, helps keep audit costs at a reasonable level, and helps avoid misunderstandings with the client.

It addresses the specifics of what, where, who, when and how:

- What are the audit objectives?
- Where will the audit be done? (i.e. scope)
- When will the audit(s) occur? (how long?)
- Who are the auditors?
- How will the audit be done?

Benefits of Audit Plan

- It helps the auditor obtain sufficient appropriate evidence for the circumstances
- It helps to keep audit costs at a reasonable level.
- It helps to avoid misunderstandings with the client.
- It helps to ensure that potential problems are promptly identified
- It helps to know the scope of audit program by an Auditor.

OBJECTIVES OF PLANNING FOR THE AUDIT

Planning for the audit is a vital area of the audit primarily conducted at the beginning of audit process to ensure that the:

- Appropriate attention is devoted to important areas
- Potential problems are promptly identified
- Work in completed expeditiously
- Work is properly coordinated

The plan developed needs to be revised as necessary during the course of audit
TYPES:

Overall Plan

It’s the general strategy for audit, which sets the direction for audit, describe the expected scope and conduct of audit and provides guiding for the development of audit programme.

Audit Programme

Detailed set of instructions to implement overall plan for the nature, timing and extent of audit procedure.

General Planning Matters

The following administrative details of an audit should be considered while developing audit plan.

1. Logistics
2. Use of IT
3. Time budgets
4. Subsidiary objectives of the assignment
5. Logistics

When planning an audit engagement partners or manager has to considers many practical areas like

1. Staff
2. Client management
3. Location of the audit
4. Dead lines

Staff

For the selection of audit staff for a particular assignment following considerations should be made.

1. Appropriate level of qualification
2. Reasonable experience and expertise
3. Availability of staff
4. Relationships with client and within staff members
5. Boarding and lodging requirements

Client Management

The management of the client may have preferences regarding audit staff. Audit manager should consider their recommendations in the light of independence rule to decide the changing of audit team as consistency of audit staff helps audit efficiency.
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TOPIC 3

INTERNAL CONTROL SYSTEM

DEFINITION OF INTERNAL CONTROL AND INTERNAL CONTROL SYSTEMS

Internal control is the process, effected by an entity's Board of Trustees, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- a. Reliability of financial reporting,
- b. Effectiveness and efficiency of operations, and
- c. Compliance with applicable laws and regulations.

Internal Control Systems are basic management practices that usually involve two elements: a policy establishing what should be done and procedures used to support the policy. Internal control systems typically come from senior management's interpretation of the company's strategic initiatives, laws and regulations, or industry standards and practices.

Types of Internal Controls:

1. Detective: Designed to detect errors or irregularities that may have occurred.
2. Corrective: Designed to correct errors or irregularities that have been detected.
3. Preventive: Designed to keep errors or irregularities from occurring in the first place.

Key Internal Control Activities

Segregation of Duties

Duties are divided, or segregated, among different people to reduce the risk of error or inappropriate actions. For example, responsibilities for receiving cash or checks, preparing the deposit to the Cashier's Office, and reconciling the deposit to the cashier's receipt and Balances should be separated.

Structure

Organizational structure - lines of authority and responsibility - should be clearly defined so that employees know where to go to report performance of duties, problems and questions related to position and the organization as a whole. An organization chart is a good means of defining this structure as long as it is kept up to date. Part of the structure is also the rules that employees must abide by. Written policies and procedures provide guidance to employees in carrying out their
duties, provide for clear rules on allowable and expected activity, as well as provide means for enforcement. The department's lines of authority and policies and procedures should be reviewed periodically to ensure they are in agreement with the organization's strategic mission.

**Authorization and Approval**

Transactions should be authorized and approved to help ensure the activity is consistent with departmental or institutional goals and objectives. For example, a department may have a policy that all purchase requisitions and invoice vouchers must be approved by the director. The important thing is that the person who approves transactions must have the authority to do so and the necessary knowledge to make informed decisions.

**Reconciliation and Review**

Performance reviews of specific functions or activities may focus on compliance, financial or operational issues. Reconciliation involves comparing transactions or activity recorded to other sources to help ensure that the information reported is accurate. For example, revenue and expense activity recorded on accounting reports should be reconciled or compared to supporting documents to ensure that the transactions are recorded timely, in the correct account, and for the right amount.

**Security**

Security may be physical or electronic (information system controls) or both. Equipment, inventories, cash, checks and other assets should be secured physically, and periodically counted and compared with amounts shown on control records. For example, the periodic physical confirmation of equipment by individual departments is a physical security control. Virus detection software should be current and updated regularly to help protect integrity of systems. Hardware and access controls (passwords) should be changed periodically and rigorously safeguarded to protect from unauthorized access to database, computer systems, etc. Special physical and software controls (such as encryption software) should be developed for systems containing sensitive and/or confidential information.

**PURPOSE OF INTERNAL CONTROL SYSTEMS**

Internal Control objectives are desired goals or conditions for a specific event cycle which, if achieved, minimize the potential that waste, loss, unauthorized use or misappropriation will occur. They are conditions which we want the system of internal control to satisfy. For a control objective to be effective, compliance with it must be measurable and observable.

Internal Audit evaluates Mercer's system of internal control by accessing the ability of individual process controls to achieve seven pre-defined control objectives. The control objectives include authorization, completeness, accuracy, validity, physical safeguards and security, error handling and segregation of duties.
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DEFINITION OF ERROR AND FRAUD

Misstatements in the financial statements can arise from fraud or error.

The term "error" refers to an unintentional misstatement in financial statements, including the omission of an amount or a disclosure, such as:

- a mistake in gathering or processing data from which financial statements are prepared;
- an incorrect accounting estimate arising from oversight or misinterpretation of facts; and
- a mistake in the application of accounting principles relating to measurement, recognition, classification, presentation, or disclosure.

- The term "fraud" refers to an intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage. Although fraud is a broad legal concept, the auditors are concerned with fraudulent acts that cause a material misstatement in the financial statements. Misstatement of the financial statements may not be the objective of some frauds. Auditors do not make legal determinations of whether fraud has actually occurred. Fraud involving one or more members of management or those charged with governance is referred to as "management fraud"; fraud involving only employees of the entity is referred to as "employee fraud". In either case, there may be collusion with third parties outside the entity.

- Two types of intentional misstatements are relevant to the auditors' consideration of fraud - misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets.

- Fraudulent financial reporting involves intentional misstatements or omissions of amounts or disclosures in financial statements to deceive financial statement users. Fraudulent financial reporting may involve:

  - deception such as manipulation, falsification, or alteration of accounting records or supporting documents from which the financial statements are prepared;
b) misrepresentation in, or intentional omission from, the financial statements of events, transactions or other significant information; and
c) intentional misapplication of accounting principles relating to measurement, recognition, classification, presentation, or disclosure.

➢ Misappropriation of assets involves the theft of an entity's assets. Misappropriation of assets can be accomplished in a variety of ways (including embezzling receipts, stealing physical or intangible assets, or causing an entity to pay for goods and services not received); it is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing.

➢ Fraud involves motivation to commit fraud and a perceived opportunity to do so. Individuals might be motivated to misappropriate assets, for example, because the individuals are living beyond their means. Fraudulent financial reporting may be committed because management is under pressure, from sources outside or inside the entity, to achieve an expected (and perhaps unrealistic) earnings target - particularly since the consequences to management of failing to meet financial goals can be significant. A perceived opportunity for fraudulent financial reporting or misappropriation of assets may exist when an individual believes internal control could be circumvented, for example, because the individual is in a position of trust or has knowledge of specific weaknesses in the internal control system.

➢ The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement in the financial statements is intentional or unintentional. Unlike error, fraud is intentional and usually involves deliberate concealment of the facts. While the auditors may be able to identify potential opportunities for fraud to be perpetrated, it is difficult, if not impossible, for the auditors to determine intent, particularly in matters involving management judgement, such as accounting estimates and the appropriate application of accounting principles.

THE DIFFERENCE BETWEEN FRAUD AND ERROR

The key distinguishing factor between fraud and error is whether the underlying action that results in a misstatement of the financial statements is intentional or unintentional. The term ‘fraud’ is a broad legal concept, but the auditor is concerned with fraud that causes a material misstatement in the financial statements. ISA 240 defines fraud as: ‘An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.’ ISA 240
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TOPIC 5

AUDIT EVIDENCE

NATURE AND SOURCE OF AUDIT EVIDENCE

Audit evidence refers to the information obtained by the auditor in arriving at the conclusions on which audit opinion on the financial statements is based. Audit evidence comprises of source documents and accounting records underlying the financial statements. The accounting records generally include:

- Records of initial entries and supporting records
- Records of electronic fund transfers, invoices, contracts and cheques.
- General and subsidiary ledgers, journal entries and other adjustments to the financial statements not reflected in the journal entries
- Records such as work sheets and spread sheets supporting cost allocations, computations and reconciliations.

Other information the auditor can use as audit evidence are:

- Minutes of meetings
- Confirmations form third parties
- Analysis reports
- Comparable data about competitors.
- Control annuals.
- Information obtained by auditor from audit procedure such as observation and enquiries.

The sources and amount of evidence needed to achieve the required level of assurance is determined by the auditor’s judgment. The auditor’s judgment will be influenced by the materiality of item being examined, the relevance and reliability of evidence available from each source and cost involved in obtaining it. Audit evidence is obtained through an appropriate mix of tests of controls and substantive procedures where internal control system is considered weak; evidence may be obtained entirely from substantive procedures.

Substantive tests are procedures carried out to test the accuracy and validity of accounting records. They are of two types i.e. analytical review procedure and test of detail.
Characteristics of reliable evidence

The evidence must be both competent and sufficient. Competence means that the evidence must be believable or worthy of trust. The seven characteristics of competent evidence include:

1. **Relevance**—to the audit objective that the auditor is testing;
2. **Independence of the provider**—information received from outside the entity is presumed to be more reliable than from inside the entity.
3. **Effectiveness of the client's internal controls**—evidence from a client whose internal controls are effective is more trustworthy.
4. **Auditor's direct knowledge**—data or calculations prepared by someone inside the organization will not be as reliable as data computed or discovered by the auditor directly.
5. **Qualifications of the individuals providing the information**—reliability of the information is enhanced if the person providing it is qualified to do so.
6. **Degree of objectivity**—objective evidence is more reliable than evidence that is subjective.
7. **Timeliness**—data that are timely for the purpose intended are considered more reliable.

Sufficiency of evidence refers to the quantity of evidence. In part, sufficiency relates to the sample size that the auditor selects, but the individual items selected for the sample may have a bearing as well.

**TYPES OF AUDIT EVIDENCE**

In deciding which procedures to use, the auditor may choose from seven different types of evidence:

1. **Physical examination**

   This is the inspection or count by the auditor of a tangible asset.

   Most often associated with inventory and cash, but it is also applicable to the verification of securities, notes receivable and tangible fixed assets.

2. **Confirmation**

   This is the receipt of a direct written response from a third party verifying the accuracy of information that was requested by the auditor.

   The request is made to the client, and the client asks the third party to respond directly to the auditor.

3. **Documentation**

   This is the auditor's inspection of the client's documents and records to substantiate the information that is, or should be, included in the F/S.
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TOPIC 6

RISKBASED AUDIT

Audit risk means the risk that the auditor may give an inappropriate audit opinion i.e. the auditor may report that the financial statements show a true and fair view while in reality they are materially misstated.

RISK-BASED AUDIT

A risk-based audit approach is designed to be used throughout the audit to efficiently and effectively focus the nature, timing and extent of audit procedures to those areas that have the most potential for causing material misstatement(s) in the financial report. ASA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment and ASA 330 The Auditor’s Responses to Assessed Risks are auditing standards that specifically set out the riskbased audit approach, with other auditing standards containing specific risk-related principles and procedures appropriate to their subject matter.

The risk-based approach requires the auditor to first understand the entity and its environment in order to identify risks that may result in material misstatement of the financial report. Next, the auditor performs an assessment of those risks at both the financial report and assertion levels. The assessment involves considering a number of factors such as the nature of the risks, relevant internal controls and the required level of audit evidence.

The result of the assessment effectively categorises the audit into a) areas of significant risk of material misstatement that require specific responses and b) areas of normal risk that can be addressed by standard audit work programs. Having assessed risks, the auditor then designs appropriate audit responses to those risks in order to obtain sufficient appropriate audit evidence on which to conclude. Risk assessment continues throughout the audit and the audit plan and procedures are amended where a reassessment is necessary. So let’s work through these key steps in more detail.

Step 1: First comes understanding

In order to identify risks that are relevant to the audit of the financial report, the auditor needs to obtain an appropriate understanding of the entity and the environment (including internal control) in which it operates. An experienced auditor’s professional skill and judgement is exercised in focusing on what specific information should be obtained through this process. Using that experience, the auditor reduces the potential for unnecessary information or information overload, by obtaining only information directly related to the financial report audit process – saving critical time and resources.

Understanding the entity includes understanding and documenting its nature, industry, ownership structure, regulatory environment, competitors, structure, key financial reporting processes and its internal control environment. Information is obtained through enquiry of relevant persons,
observation and inspection of processes and documentation, and performing analytical procedures on key financial and non-financial information.

Understanding the entity’s internal control framework is often seen as problematic for auditors, particularly in knowing what controls to focus on, and what type of information, and how much information, to obtain on the controls. Auditors need to understand those controls (individually or in combination) that are considered likely to be relevant to the audit (for example controls related to financial reporting) – not all the controls the entity employs in managing its business.

The control framework assists auditors to focus on obtaining an understanding of relevant controls by dividing the entity’s internal controls into five components:

- Control environment: the control culture of the entity and its impact
- Entity’s own risk assessment process: how the entity identifies, assesses and responds to its own business risks
- Information systems relevant to the financial reporting: those systems related to the capture of significant transactions, events, conditions or accounting estimates, the procedures related to nonstandard journal entries, reconciliations of sub-ledgers to the general ledger, the data entry of transactions, and reporting in the financial report
- Control activities relevant to audit: those policies and procedures that help ensure that management directives are carried out (ie control activities designed to prevent/detect misstatements). Examples of control activities include those relating to authorisation, performance reviews, information processing, physical controls and segregation of duties
- Monitoring of control activities: those activities the entity uses to monitor control activities over financial reporting, as well as how it takes action to address any identified deficiencies.

Understanding internal control in this way enables the auditor to identify what relevant controls (if any) are in place to test, whether the absence of controls creates risk, how or when to combine controls testing with substantive testing, how to test the operating effectiveness of controls and the extent of reliance that can be placed on internal controls (thereby reducing the extent of substantive testing).

**Step 2: With understanding comes identifying and assessing risk**

The auditor’s understanding of the entity’s financial reporting environment enables the auditor to identify those risks that potentially affect the overall financial report or individual transactions, account balances and disclosures within it (at the assertion level). Considerable professional judgement and skill are required to not only identify such risks but also to relate how they potentially impact the recognition, measurement, presentation and disclosure in the financial report or the valuation, allocation, occurrence, completeness, accuracy, cut-off, classification, existence, or rights and obligations at the assertion level. The nature of the risk will also determine how the auditor designs the audit work program (for example, through a combination of controls testing and substantive testing or substantive testing only).

The initial risk assessment is performed at the audit planning stage, with it being reassessed and revised if new risks are identified during the audit. The auditor exercises professional judgement in
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TOPIC 7

COMPUTERISED AUDITING

BENEFITS AND DRAWBACKS OF COMPUTERIZED ACCOUNTING SYSTEMS:

BENEFITS

1. **Speed** — data entry onto the computer with its formatted screens and built-in databases of customers and supplier details and stock records can be carried out far more quickly than any manual processing.
2. **Automatic document production** — fast and accurate invoices, credit notes, purchase orders, printing statements and payroll documents are all done automatically.
3. **Accuracy** — there is less room for errors as only one accounting entry is needed for each transaction rather than two (or three) for a manual system.
4. **Up-to-date information** — the accounting records are automatically updated and so account balances (e.g. customer accounts) will always be up-to-date.
5. **Availability of information** — the data is instantly available and can be made available to different users in different locations at the same time.
6. **Management information** — reports can be produced which will help management monitor and control the business, for example the aged debtors analysis will show which customer accounts are overdue, trial balance, trading and profit and loss account and balance sheet.
7. **GST/NAT return** — the automatic creation of figures for the regular GST/VAT returns.
8. **Legibility** — the onscreen and printed data should always be legible and so will avoid errors caused by poor figures.
9. **Efficiency** — better use is made of resources and time; cash flow should improve through better debt collection and inventory control.
10. **Staff motivation** — the system will require staff to be trained to use new skills, which can make them feel more motivated. Further to this with many 'off-the-shelf packages like MYOB the training can be outsourced and thus making a particular staff member less critical of business operations.
11. **Cost savings** — computerized accounting programs reduce staff time doing accounts and reduce audit expenses as records are neat, up-to-date and accurate.
12. **Reduce frustration** — management can be on top of their accounts and thus reduce stress levels associated with what is not known.
13. **The ability to deal in multiple currencies easily** — many computerized accounting packages now allow a business to trade in multiple currencies with ease. Problems associated with exchange rate changes are minimized.
DRAWBACKS

1. Power failure, computer viruses and hackers are the inherent problems of using computerized systems;

2. Once data been input into the system, automatically the output are obtained hence the data being input needs to be validated for accuracy and completeness, we should not forget concept of GIGO (Garbage In(Input) Garbage out (Output)) and

3. Accounting system not properly set up to meet the requirement of the business due to badly programmed or inappropriate software or hardware or personnel problems can caused more havoc and

4. Danger of computer fraud if proper level of control and security whether internal and external are not properly been instituted.

A computer system requires procedures to;

- Convert data to machine readable form.
- Input data into the computer.
- Process data.
- Store data in machine readable form.
- Convert data into desired output form.

For these procedures to be undertaken, a mixture of hardware and software is needed. The hardware will consist of;

i. Input devices. These include keyboards, optical readers, and bar code scanners.
ii. Processing devices. These are the computers themselves. i.e. CPU
iii. Storage devices include hard disk, diskettes and magnetic tapes.
iv. Output devices. These include the visual display unit (VDU) and printers.

The computer software consists of programs and operating systems.

Programs are the instructions telling the computer how each type of transaction is to be processed. These instructions include routines of checking and controlling data, matching data with master files and performing mathematical operations on data. E.g. for sales transactions, matching routines will enable the computer to identify the right sales price from the sales master file and the right customer from debtors master file. Mathematical routines will include calculating the total debtor’s amount and updating customer’s balance in the debtors’ master file.
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TOPIC 8
AUDIT REPORT

INTRODUCTION

An audit report is a written opinion of an auditor regarding an entity's financial statements. The report is written in a standard format, as mandated by international standard reporting.

An audit report may also be described as an appraisal of a business’s complete financial status. Completed by an independent accounting professional, this document covers a company’s assets and liabilities, and presents the auditor’s educated assessment of the firm’s financial position and future. Audit reports are required by law if a company is publicly traded or in an industry regulated by the Securities and Exchange Commission. Companies seeking funding, as well as those looking to improve internal controls, also find this information valuable. There are four types of audit report.

Companies Act stipulates the statements that should be expressly stated in the auditor’s report. These are;

1. Whether they have obtained all the information and explanations which to the best of their knowledge and belief were necessary for the purposes of their audit.
2. Whether in their opinion, proper books of account have been kept by the company, so far as appears from their examination of those books, and proper returns adequate for the purposes of their audit have been received from branches not visited by them.
3. Whether the company's balance sheet and (unless it is framed as a consolidated profit and loss account) profit and loss account dealt with by the report are in agreement with the books of account and returns.
   - Whether, in their opinion and to the best of their information and according to the explanations given to them, the said accounts give the information required by this Act in the manner so required and give a true and fair view—
     (a) in the case of the balance sheet, of the state of the company's affairs as at the end of its financial year; and
     (b) in the case of the profit and loss account, of the profit or loss for its financial year; or, as the case may be, give a true and fair view thereof subject to the non-disclosure of any matters (to be indicated in the report) which by virtue of Part III of the Sixth Schedule are not required to be disclosed.
4. In the case of a company which is a holding company and which submits group accounts whether, in their opinion, the group accounts have been properly prepared in accordance with the provisions of this Act so as to give a true and fair view of the state of affairs and profit or
loss of the company and its subsidiaries dealt with thereby, so far as concerns members of the company, or, as the case may be, so as to give a true and fair view thereof subject to the non-disclosure of any matters (to be indicated in the report) which by virtue of Part III of the Sixth Schedule are not required to be disclosed.

When financial statements are finalised, they usually must contain an evaluation – an auditor's report from a licensed accountant or auditor. This report provides an overview of the evaluation of the validity and reliability of a company or organization’s financial statements.

PURPOSE OF THE AUDITORS REPORT

The main purpose of an auditor's report is to document reasonable assurance that a company’s financial statements are free from error.

An audit of a company’s financial statements should result in a report wherein the accountant or auditor is free to share their opinion about the validity and reliability of a company’s financial statements.

In this report, the auditor should provide an accurate picture of the company and their financial statements. The auditor should also state whether they are externally or internally connected to the company.

Within the report, the auditor can share any reservations about the condition of the company’s finances or relevant additional information. Reservations could arise if the auditor disagrees with something found in the financial statements, e.g. if the auditor disagrees with management about the valuation of an asset because they believe that this has a more significant impact on the financial statements.

In the report there are rules concerning what an auditor's report should include and the order in which various items should be reported.

Auditor's reports must adhere to accepted standards established by governing bodies. The governing bodies help to assure external users that the auditor's opinion on the fairness of financial statements is based on a commonly accepted framework.

ELEMENTS OF THE AUDITORS REPORT

Basic elements of auditor's report
The Companies Act does not stipulate the form the auditor's report should take. The auditing standards seek to ensure that the auditor's report is clear and unambiguous. To this end, it seeks to standardize the form of the auditor's report.
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TOPIC 9

PROFESSIONAL ETHICS

Professional ethics are professionally accepted standards of personal and business behaviour, values and guiding principles. Codes of professional ethics are often established by professional organizations to help guide members in performing their job functions according to sound and consistent ethical principles.

IMPORTANCE OF PROFESSIONAL ETHICS

The purpose of assurance engagements is to increase the confidence of end users of information by reducing their level of risk. It therefore follows that the user needs to trust the professional who is providing the assurance. In order to be trusted the auditor needs to be independent of their clients and be sufficiently competent and diligent to complete their assignments satisfactorily.

The last thirty years has witnessed a number of high profile corporate scandals that have had far reaching implications for companies, economies and accountancy firms.

To improve the image of the profession and to restore trust between users of accountancy services and the practitioners, it is vital that accountants operate (and are perceived to operate) according to an accepted code of ethics.

Whilst it is expected that practitioners apply the spirit of the code to every day practice the framework and principles would be of little use if they could not be enforced.

Business organizations often develop several different policies, rules and guidelines for governing their operations. While home-based or sole proprietorship businesses usually require fewer policies, larger organizations use these guidelines to manage employee behavior. A code of ethics is a common organizational policy used in business organizations. The code of ethics policy usually sets the minimum standards for business owners, managers and employees to follow when completing various business functions.

Facts

In a small business, a code of ethics is usually based on the business owner’s personal morals or values. As the business grows and expands, the ethical values can be implemented into the business' organizational mission or values statement. This statement helps provide companies with a compass to guide the organization through the business environment. Companies often refer to the mission or values statement when guidance is needed regarding questionable situations.
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