FINANCIAL AUDIT MANAGEMENT

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Abstract

Financial audit expresses, as its main aim, an opinion on the extent to which the financial statements present a true and fair view of the entity's economic affairs at the balance sheet date and the results for the year ended, in compliance with the laws in force and practices in the country where the entity is established.

To achieve this objective, the audit process requires an examination management and methodology to ensure an independent opinion, so as to equally protect all the users of the accounting information: shareholders / partners, state, employees, banks, debtors, customers, suppliers etc.

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1. Introduction

Every audit mission involves an efficient management to bring a plus of value to the audited entity.

An audit mission is a separate and identifiable activity which is completed when the auditor issues *a point of view*, *statements* or *opinions* recorded in a report on an entity's accomplishment of some clear and well defined aims. While carrying out the audit, the auditor must have a reasoned opinion on the following two aspects: the validity and mechanism of the internal procedures, approved by the entity's management, regarding its internal control, internal audit and appropriate, clear and complete image of its transactions and other events that are materialized in assets, liabilities and equity belonging to the entity at the reporting date.

2. Analysis of the financial audit model

Regardless of its objectives, an audit mission can be regarded as a system that includes the following steps, each being after a particular model:

a. *precondition (preplanning);*

b. *planning;*

c. *working;*

d. *reporting;*

e. *post reporting*.

Planning the audit

By *planning* we understand building a general strategy and a detailed approach regarding the nature, duration and extent of the audit mission. The effectiveness of an audit mission depends exactly on how the planning is done.

International Standards on Auditing 300, "Planning an audit of financial statements", refers to the auditor's responsibility to plan an audit of the financial statements. The auditor's objective is to plan the audit so as to be conducted in a more efficient manner.

Planning varies from one entity to another, depending on its size, complexity of the audit, the auditor's experience and knowledge of the work undertaken by the entity.

Audit planning, materialized on the mission, includes its two first stages, namely the *preliminary stage* or *the preplanning and the planning stage*.

The preliminary or preplanning stage of the audit mission includes the following activities to be conducted by the auditor:

• understanding the audited entity;

• preliminary assessment of the internal control and accounting system;

• defining the objectives of the audit;

• initial assessment of the needed resources and the establishment of the auditing schedule.

The planning stage

ISA 300 *Planning an audit of the financial situations* establishes standards and provides instructions regarding the considerations and activities applicable to planning the financial audit. ISA 300 establishes detailed planning processes that an auditor should run.

In short, the planning activities should include:

a. establishing a *general strategy of audit*;

b. developing an *audit plan* to reduce audit risk to an acceptable low level;

c. continuous *updating of the general audit strategy* and *the audit plan* during the audit mission;

d. *communicating with those charged with governance and management (of the entity* that is audited).

Establishing the audit strategy

Firstly, the auditor establishes *a general audit strategy*, which sets the scope, time and management of the audit, which will provide the basis for *the audit plan.* At the *general audit strategy* stage, the auditor conducts the following activities:

• identifying the characteristics of the audit mission and defining its coverage;

• evaluating the audit mission's objectives of the reporting in order to plan the period for conducting the audit and the nature of the required communications;

• identifying the factors which, based on the auditor's professional reasoning, are significant for effectively helping the audit team;

• taking into consideration the results of the preliminary audit mission and the knowledge accumulated in previous audits;

• establishing the nature, period and level of resources necessary to carry out the mission.

Elaborating the audit plan

Based on the general strategy of audit, the auditor develops an *audit plan*. Before starting the detailed planning of the audit, it is imperative that the auditor acquire extensive knowledge of entity's activity. This is necessary because it would be impossible to achieve a solid evaluation of the level of risks without fully understanding the entity and its business environment. So the audit plan includes the strategy to be followed in carrying out the mission, based on the auditor's understanding of the client's activity characteristics and the audit risks arising from them.

The audit plan includes the following:

a. the nature, extent and period of the assessment procedures of the planned risks, as provided by the International Standards on Auditing ISA 315 "Understanding the entity and its environment and assessing the risks of material misstatements";

b. the nature, period and extent of the subsequently planned procedures of the audit, at the level of allegations, according to the International Standards on Auditing 330, "The auditor's procedures in response to assessed risks";

c. other planned audit procedures that should be made so that the mission is in accordance with the international auditing standards in question.

The *audit plan* is also the framework according to which the resources of the audit mission (hours / man) are assigned to different stages (parts) of the commitment.

For the documentation of the audit plan the entity will pursue the following procedures:

a) knowing the audited entity's business activities;

b) assessment of the audit risk and its components;

c) establishment of samples;

d) evaluation of accounting estimates made by management;

e) analysis of errors and fraud;

f) calculation of the threshold of significance;

g) assessment of the principle of going concern;

h) conducting a preliminary analytical procedures.

Knowing the entity's activity is a continuous and cumulative process of gathering and evaluating information, which includes both an analysis of the general economic factors and the conditions specific to the economic activity that affect the audited entity and the management's competence level.

The preliminary conduct of analytical procedures is a prerequisite for understanding the activity and identifying the areas of potential risk. The auditor is required that, while acquiring knowledge of the business entity's activity, to conduct a preliminary analysis of the balance sheet, the risk indicators, liquidity, activity, profitability and results, information which will lead to understanding the financial information.

Preliminary assessment of the principle of going concern. The financial audit depends on the preliminary assessment of business continuity. Where business continuity is no longer safe, the auditor will examine all areas on which this would have an impact (International Standards on Auditing 570, "The going concern principle").

Calculation of the threshold of significance. The relevance of the financial information is equally affected by the threshold of significance of that piece of information. Determining the threshold of significance is a subjective activity, and the auditor should use their professional reasoning in evaluating this, because, in practice, it is improper to define it by a mathematical formula, as long as it aims at both quantitative aspects and qualitative aspects.

Analysis of possible fraud and errors.

Checking accounting estimates made by management. A part of the financial statements can not be measured accurately, but only estimated. "Accounting estimation is an approximation of the value of an item in the absence of precise methods of estimation". In order to express an appropriate opinion, the auditor must develop an independent model of evaluation of the estimates and compare the obtained results with the accounting estimates made by entity's management. Where there is a difference between the auditor's assessment and the estimated amount included in the financial statements, the auditor must determine to what extent this difference requires an adjustment.

Evaluation of the audit risk and of its components. The assessment of risk is an important step of any audit tasks. The approach of this evaluation is presented in the Minimum audit norms, F1-F3 sheets, the assessment of general inherent risk being based on a set of questionnaires, each question being asked in such a way that the YES answer represents a risk index, the ultimate goal being the determination of the sample size.

Finding the level of sampling and selection of these samples. Based on data gathered by the auditor at this stage, the nature and scope of the work to be carried out by the auditor during the mission will be determined and organizational measures necessary for their performance in terms of maximum efficiency will be established.

The audit program

The auditor develops *audit programs* as part of the audit plan which set out the nature, duration and extent of the planned audit procedures required to implement the audit plan.

The audit program consists of a set of instructions addressed to the members of the audit team and a means to record and control the audit activity.

The program also includes the objectives for each area and a timetable for each area of the audit procedure.

Continuous upgrading of the general audit strategy and audit plans

In practice, it was found that there aren't two identical audit missions. Therefore, the audit strategy and the detailed planning procedures for auditing the entity's financial statements will differ from those performed in any other audit. Finding an audit strategy and audit planning are (in general) dynamic processes and the auditors should be aware that it is possible that the audit procedures, which are part of the initial strategy or plan, may not be implemented or, conversely, may be extended as a result of the initial test results. For example, during an audit the auditor can discover that fraudulent activity was carried out by a director of the company. This may probably lead to a change in the strategy for what remained of the conducted audit.

Communicating with those charged with governance and management

The auditors should bear in mind that, regardless of any regulatory directive, they should communicate with the directors in relation to the audit planning. Communication is necessary to improve *efficiency and effectiveness of the audit*. The members of the audit team who communicate with the audited entity's governance should be aware that managers should not have any influence on the audit strategy or audit plan.

An audit mission can not achieve its role if the audit team does not thoroughly understand the following elements:

- the overall objectives of the audit;
- the responsibilities the auditor has during its mission;

- the specific objectives that the auditor tries to reach.

Without understanding these issues, planning the audit and collecting the elements proved throughout the mission will have no relevance.

Working stage (application of substantive procedures for gathering the audit samples)

To understand the importance of gathering the proving elements, the auditor must define the following specific objectives of the audit mission:

- understanding the auditor's objectives and responsibilities;
- segmentation of financial situations in cycles;
- requesting the management their statements on the accounts;
- knowledge of the general objectives of the audit regarding the categories of transactions and accounts;
- knowledge of the specific objectives of the audit regarding the categories of transactions and accounts.

An audit mission on financial statements involves their segmentation into smaller and, as far as possible, homogeneous parts. This segmentation allows a more efficient management of the audit mission, thus facilitating a rational allocation of tasks to audit team members. In audit practice one can meet different *methods of segmentation* of an audit tasks. An effective method, widely spread in the professional practice, consists of the *employment, in the same segment, of the types of transactions and account balances closely correlated*. This technique is known as *the method of cycles*. Thus there are the following groups of cycles:

- the sales - receipts cycle;
- the buying- payments cycle;
- the staff remuneration cycle;
- the stocks - storage cycle;
- the capital operations cycle.

According to the method of cycles, auditors perform audit missions by applying audit tests on transactions constituting the final sold of the accounts. From the practice of auditing one thing has resulted that *the most effective auditing method of the accounts is to obtain a certain combination of insurance on each transaction as well as the final sold of the account associated with those operations*. From the above, we can draw the conclusion that the auditor should follow the following objectives:

- audit objectives related to transactions;
- audit objectives related to sold;
- audit objectives related to the management's statements.

After the auditor goes through all procedures for each account of the financial situations, the obtained information should be gathered and analyzed in order to draw an overall conclusion regarding the accurate picture presented in the financial statements. When the mission ends, the auditor issues *an audit report* which must meet a number of technical conditions.

The Reporting Stage

The final result of the audit work is for the audit coordinator to develop or approve *an audit report* on the financial statements, based on the obtained results and conclusions in which the opinion is clearly expressed.

The auditors have the legal obligation to make a report to shareholders on the accounts examined by them and on the balance sheet and the profit and loss.

The auditors' report must say whether, in their opinion, the financial statements give a true and fair view of the financial position of the entity at the time of reporting, of the entity's results of its activities and cash flows for the audited period, in accordance with the regulations.

According to the national standards, the audit report may take one of the following forms:

1. *standard financial report*, which contains *an opinion without reservations*.
2. *amended financial audit report*, which, depending on the seriousness of the encountered situation, may be:

a) *report without reservations*, but with a separate paragraph;

b) *report with reservations*;

c) report which contains the refusal to express an opinion (*the impossibility of expressing an opinion*);

d) report with unfavorable opinion (*contrary opinion*).

3. Conclusion

The audit report therefore represents the final stage of the audit mission, the product of the auditor's work, which presents the final conclusions following the examination of an entity's financial information of, the auditor's opinion, the financial statements being prepared or not, in all significant respects, in accordance with an applicable financial reporting framework. Although the auditors are not guarantors or institutions that offer absolute assurance of the accuracy of the accounting information contained in the financial statements, they assume an important responsibility regarding the need to inform the users if their financial situations are credible or not. All those mentioned in this article emphasize the role of the financial audit management throughout the financial conduct of the audit mission.

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