IT AUDITING SE5106

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BASICS

- Recent developments in information technology (IT) have had a tremendous impact on the field of auditing
- Business organizations undergo different types of audits for different purposes. The most common of these are
  - *external (financial) audits*
  - *internal audits*
  - *fraud audits*

1. EXTERNAL (FINANCIAL) AUDITS

- An external audit is when an independent expert checks and verifies the accuracy and fairness of a company's financial records and statements.
  - the auditor — who expresses an opinion regarding the presentation of financial statements.
- It (task) is known as the attest service, is performed by Certified Public Accountants (CPA) who work for public accounting firms that are independent of the client organization being audited.
- The audit objective is always associated with assuring the fair presentation of financial statements.

1. EXTERNAL (FINANCIAL) AUDITS

- A key concept in this process is independence.
- Public confidence in the reliability of the company's internally produced financial statements rests directly on an evaluation of an independent auditor.

Refer - *Attest Service versus Advisory Services*

1. EXTERNAL (FINANCIAL) AUDITS

- Financial Audit Components
  - *Auditing Standards*
  - *A Systematic Process*
  - *Management Assertions and Audit Objectives.*
  - *Obtaining Evidence*
  - *Ascertaining Materiality*
  - *Communicating Results*

2. INTERNAL AUDITS

- The Institute of Internal Auditors (IIA) defines internal auditing as an independent appraisal function established within an organization to examine and evaluate its activities as a service to the organization

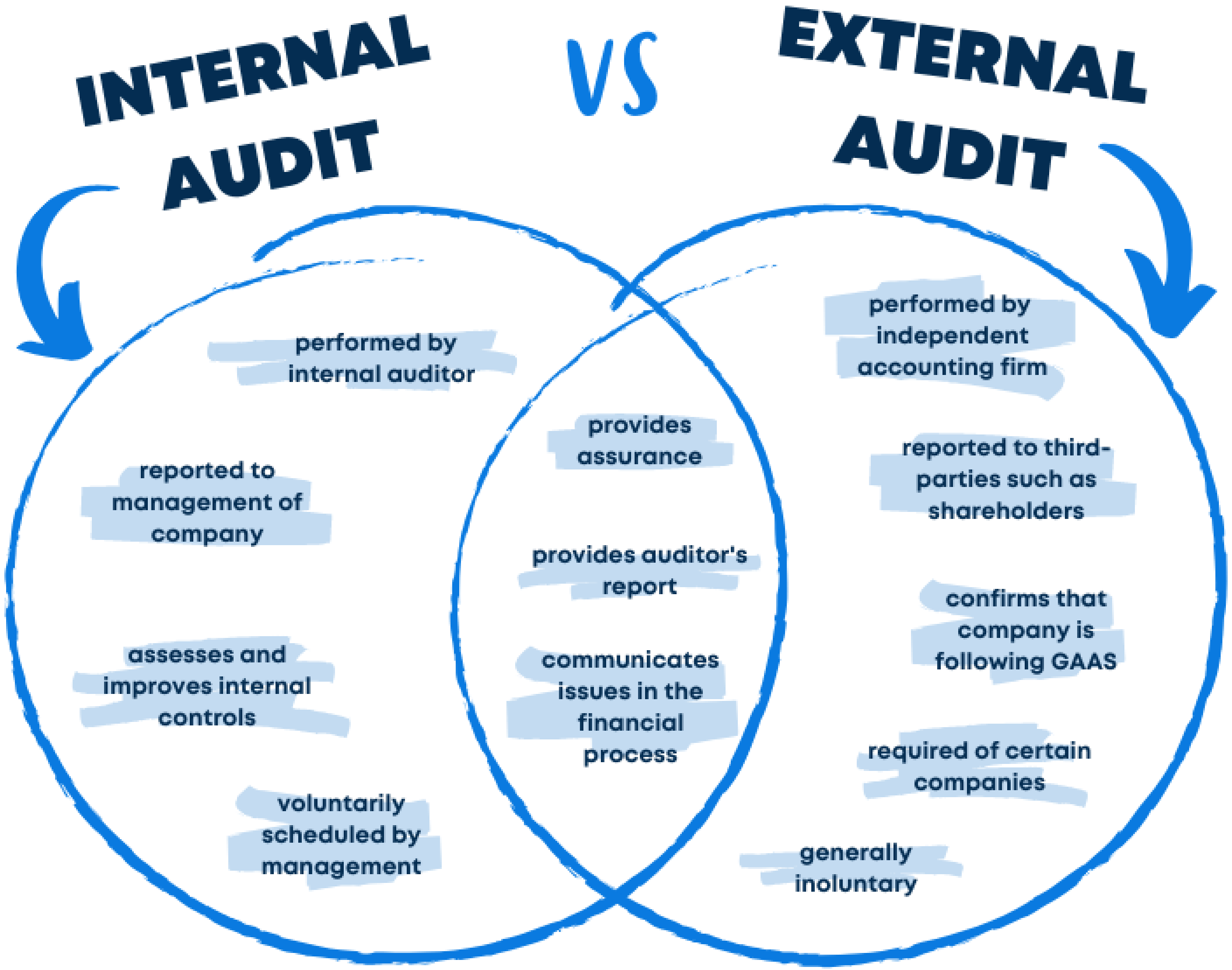
2. INTERNAL AUDITS

- Internal auditors perform a wide range of activities on behalf of the organization, including
  - *conducting financial audits,*
  - *examining an operation’s compliance with organizational policies,*
  - *reviewing the organization’s compliance with legal obligations,*
  - *evaluating operational efficiency, and*
  - *detecting and pursuing fraud within the firm.*

2. INTERNAL AUDITS

- An internal audit is typically conducted by auditors who work for the organization, but this task may be outsourced to other organizations.

Refer - *External versus Internal Auditors*


INTERNAL AUDIT
VS
EXTERNAL AUDIT
performed by internal auditor
reported to management of company
assesses and improves internal controls
voluntarily scheduled by management
provides assurance
provides auditor's report
communicates issues in the financial process
performed by independent accounting firm
reported to third-parties such as shareholders
confirms that company is following GAAS
required of certain companies
generally inoluntary

3. FRAUD AUDITS

- In recent years, fraud audits have, increased in popularity as a corporate governance tool.

- The objective of a fraud audit is to investigate anomalies and gather evidence of fraud that may lead to criminal conviction.

THE ROLE OF THE AUDIT COMMITTEE

- The board of directors of publicly traded companies form a subcommittee known as the audit committee, which has special responsibilities regarding audits

- The audit committee must be willing to challenge the internal auditors (or the entity performing that function) as well as management, when necessary

- Part of its role is to look for ways to identify risk

AUDIT RISK

- Audit risk is the probability that the auditor will render an unqualified (clean) opinion on financial statements that are, in fact, materially misstated.
- Material misstatements may be caused by errors or irregularities or both. Errors are unintentional mistakes.
- Irregularities are intentional misrepresentations associated with the commission of a fraud such as the misappropriation of physical assets or the deception of financial statement users.

AUDIT RISK COMPONENTS

- The auditor's objective is to achieve a level of audit risk that is acceptable to the auditor.
- Acceptable audit risk (AR) is estimated based on the ex ante value of the components of the **audit risk model**.
- These are
  - *inherent risk,*
  - *control risk,*
  - *detection risk.*

AUDIT RISK COMPONENTS

- Inherent risk - associated with the unique characteristics of the business or industry of the client
- Control risk - the likelihood that the control structure is flawed because controls are either absent or inadequate to prevent or detect errors in the accounts.
- Detection risk - the risk that auditors are willing to take that errors not detected or prevented by the control structure will also not be detected by the auditor.

AUDIT RISK COMPONENTS

- Audit Risk Model

Acceptable Audit Risk = Inherent Risk * Control Risk * Detection Risk

THANK YOU