



Gathering Appropriate Audit Evidence

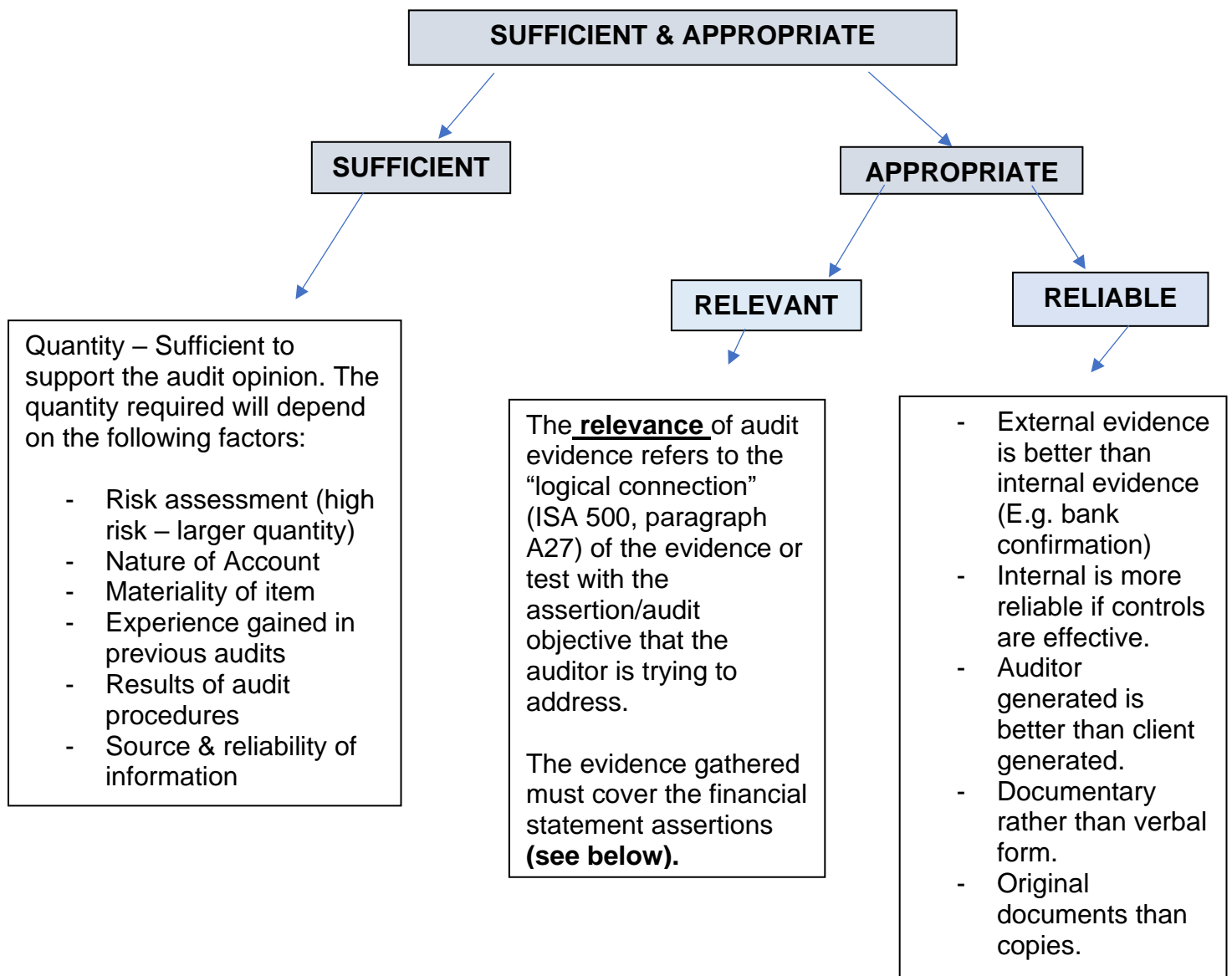
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The main purpose of an audit is for the auditor to issue an audit opinion on the financial statements. The auditor must gain evidence that supports each of the balances, transactions and disclosures in the financial statements.

ISA 500, paragraph 6, requires the auditor to “design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining **sufficient appropriate** audit evidence”.

Sufficient appropriate audit evidence:

- **Sufficient** – is the measure of the **quantity** of audit evidence. E.g. the sample chosen should be large enough to be representative.
- **Appropriateness** – is the measure of the **quality** of audit evidence. To be of good quality it should be **relevant** and **reliable**.



Financial Statement Assertions

ISA 315, states that the auditor must use assertions for **classes of transactions and related disclosures** and **account balances and related disclosures** in sufficient detail to form the basis for the assessment of risks of material misstatement and the design and performance of further audit procedures.

Assertions used by the auditor

Classes of transactions (e.g. revenue, expenses, bank transactions, fixed asset additions, etc.)	Account balances (e.g. asset, liability and equity balances in the statement of financial position)
Occurrence	Existence
Completeness	Completeness
Accuracy	Valuation
Cut-off	Rights and Obligations
Presentation/Classification and Disclosure	

Assertions about classes of transactions and events and related disclosures for the period under audit	
Occurrence	Transactions and events that have been recorded or disclosed have occurred, and such transactions pertain to the entity.
Completeness	All transactions have events that should have been recorded have been recorded, and all related disclosures that should have been included in the financial statements have been included.
Accuracy	Amounts and other data relating to recorded transactions and events have been recorded appropriately, and related disclosures have been appropriately measured and described
Cut-off	Transactions and events have been recorded in the correct reporting period.
Classification	Transactions and events have been recorded in the proper accounts.
Presentation	Transactions and events are appropriately aggregated or disaggregated and are clearly described, and related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.

Assertions about account balances and related disclosures at the period end	
Existence	Assets, liabilities and equity interests exist.
Completeness	All assets, liabilities and equity interests that should have been recorded have been recorded, and all related disclosures that should have been included in the financial statements have been included.
Valuation	Assets, liabilities and equity interests have been included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments have been appropriately measured and described.
Rights & Obligations	The entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
Classification	Assets, liabilities and equity interests have been recorded in the proper accounts.
Presentation	Assets, liabilities and equity interests are appropriately aggregated or disaggregated, and clearly described, and related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.

Audit procedures to obtain audit evidence

Auditors may obtain evidence by one of more of the following procedures:

- **Analytical Procedures** – Evaluating financial and non-financial information and comparing actual results to expectations. It is important to investigate identified fluctuations and relationships that are inconsistent with other relevant information or deviate significantly from predicted amounts.
- **Enquiry and External confirmation** – Enquiry involves seeking information from client staff or external sources. External confirmation is the process of obtaining a representation of information or of an existing condition directly from a third party e.g. confirmation from bank of bank balances, confirmation from customer of aged receivable balance at period end.
- **Inspection** - Inspection involves examining, vouching, tracing or verifying records or other documents, processes, conditions or transactions.
- **Observation** – Observation consists of looking at a process or procedure being performed by others.
- **Recalculation and reperformance** – Recalculation consists of verifying the mathematical accuracy of documents and accounting records and re-computing financial statements amounts or supporting details, including client schedules. Reperformance is the auditor's independent execution of procedures of controls.

Remember **AEIOU!**

Gathering appropriate audit evidence – Example:

*A&B Limited have motor vehicles in the financial statements at the year end of £680,000. The audit junior obtained a list of all motor vehicles and physically inspected them. The audit junior is happy that all motor vehicles **exist** at the year end.*

The above audit test only ensured the motor vehicles actually **exist**.

Consider the following:

- **Rights and obligations:** Does A&B Limited actually own the motor vehicles?
- **Completeness:** Could A&B Limited have more motor vehicles than we are aware of?
- **Valuation/Accuracy:** Is the net book value of £680,000 appropriate at the year end?
Are the motor vehicles being depreciated appropriately?
- **Classification/Presentation:** Have the motor vehicles been classified correctly?
Have they been presented accurately in the disclosure notes in the financial statements?

Conclusion:

Gathering sufficient and appropriate audit evidence is very important. This is a key syllabus area, and you must be very comfortable with the assertions.

When designing audit plans and procedures for specific areas, you must focus on the financial statement assertions that you are trying to find evidence to support.

If a question asks for audit procedures relating to a particular assertion, make sure your answer addresses only the assertion required by the question.