Auditing & Assurance Services

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Overview

Timothy Louwers's "Auditing & Assurance Services" is a comprehensive textbook designed to introduce students and professionals to the fundamental principles, concepts, and practices of auditing and assurance services. The book systematically covers the entire audit process, from initial client acceptance and planning to the issuance of the audit report. It emphasizes the critical role of auditors in enhancing the credibility of financial statements and the importance of professional skepticism, ethical conduct, and compliance with professional standards.

The text integrates theoretical knowledge with practical applications, often incorporating real-world examples, case studies, and discussions of current regulatory developments, such as those from the Public Company Accounting Oversight Board (PCAOB) and the American Institute of Certified Public Accountants (AICPA). It delves into key areas like risk assessment, internal control evaluation, audit evidence gathering, statistical sampling, and the various types of audit reports. The book also explores the broader scope of assurance services beyond traditional financial statement audits, preparing readers for the evolving landscape of the accounting profession. Its relevance lies in equipping future auditors with the necessary tools and understanding to navigate complex audit environments and uphold public trust.

Key Takeaways

- Always maintain professional skepticism throughout the audit process to critically evaluate evidence and challenge management assertions.
- Understand and apply the framework of generally accepted auditing standards (GAAS) and other relevant professional standards to ensure audit quality and compliance.
- Thoroughly assess inherent risk and control risk to effectively plan the nature, timing, and extent of substantive audit procedures.
- Evaluate the effectiveness of a client's internal controls, as strong controls can reduce the need for extensive substantive testing.
- Gather sufficient appropriate audit evidence to support audit opinions, ensuring it is both relevant and reliable.
- Recognize the ethical responsibilities of an auditor, prioritizing independence, integrity, and objectivity in all engagements.

• Master the different types of audit reports and the conditions under which each is issued, clearly communicating audit findings and opinions.

• Stay informed about the evolving regulatory environment and technological advancements impacting the auditing profession.

Chapter Summaries

Introduction to Auditing and Assurance Services

This foundational chapter defines auditing, distinguishing it from accounting, and explains the demand for independent assurance. It introduces various types of audits, such as financial statement, operational, and compliance audits, and the different types of auditors, including external, internal, government, and forensic auditors. The chapter also covers the concept of assurance services beyond traditional audits, highlighting the value they provide by enhancing the reliability of information for decision-makers. Key concepts like the agency theory and information risk are often discussed to frame the necessity of auditing in capital markets.

The Public Accounting Profession and Audit Quality

This chapter delves into the structure and regulation of the public accounting profession. It describes the different organizational forms of audit firms, from sole practitioners to large multinational networks, and discusses the roles of key regulatory bodies such as the Public Company Accounting Oversight Board (PCAOB), the American Institute of Certified Public Accountants (AICPA), and the International Auditing and Assurance Standards Board (IAASB). Emphasis is placed on the importance of audit quality, including the elements of a system of quality control within an audit firm and the peer review process designed to ensure adherence to professional standards.

Professional Ethics, Independence, and Legal Liability

This critical chapter explores the ethical framework guiding auditors, primarily focusing on the AICPA Code of Professional Conduct and its principles, including responsibility, public interest, integrity, objectivity, due care, and scope and nature of services. A significant portion is dedicated to auditor independence, detailing rules and interpretations that prevent conflicts of interest, especially for public company audits under SOX. The chapter also addresses the legal environment auditors operate in, discussing common law liability to clients and third parties, and statutory liability under federal securities acts like the Securities Act of 1933 and the Securities Exchange Act of 1934, often illustrated with landmark legal cases.

Audit Planning and Materiality

This chapter covers the initial phases of an audit engagement. It begins with client acceptance and continuance procedures, including evaluating client integrity and auditor capabilities. It then moves to establishing an understanding with the client, developing an overall audit strategy, and

preparing the audit plan. A central concept introduced is materiality, explaining how auditors determine planning materiality and allocate it to individual accounts (tolerable misstatement). The chapter also discusses the importance of identifying related parties and understanding the client's business and industry to effectively plan the audit.

Assessing and Responding to Audit Risk

This chapter details the auditor's responsibility to assess and respond to audit risk, which is the risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. It introduces the audit risk model (AR = IR x CR x DR), explaining inherent risk, control risk, and detection risk. Auditors learn how to identify and assess business risks, including fraud risks, and how these assessments influence the nature, timing, and extent of substantive audit procedures. The chapter also covers the documentation of risk assessments and the design of appropriate audit responses.

Internal Control Over Financial Reporting

This chapter focuses on understanding and evaluating a client's internal control over financial reporting. It introduces the COSO Internal Control—Integrated Framework as the benchmark for effective internal control, detailing its five components: control environment, risk assessment, control activities, information and communication, and monitoring activities. The chapter covers management's responsibilities under Sarbanes-Oxley (SOX) Sections 302 and 404, and the auditor's role in assessing control risk, performing tests of controls, and, for public companies, issuing an opinion on the effectiveness of internal control over financial reporting.

Audit Evidence and Documentation

This chapter explains the types of audit evidence auditors gather and how they document their work. It discusses the concepts of sufficiency and appropriateness of audit evidence, detailing various audit procedures used to obtain evidence, such as inspection, observation, inquiry, confirmation, recalculation, reperformance, and analytical procedures. The reliability of different types of evidence is also examined. Furthermore, the chapter emphasizes the importance of proper audit documentation, including the purpose, content, and organization of audit working papers, ensuring they provide a clear record of the work performed and the conclusions reached.

Auditing the Revenue and Collection Cycle

This chapter applies audit concepts to the revenue and collection cycle, which includes sales, accounts receivable, and cash receipts. It covers common business functions and related internal controls within this cycle. The chapter details specific audit objectives for assertions related to existence, completeness, valuation, and cutoff for revenue and receivables. It outlines various tests of controls (e.g., for sales order authorization, credit approval) and substantive procedures (e.g., confirmations of accounts receivable, cutoff tests for sales and cash receipts, analytical procedures for revenue accounts) designed to gather sufficient appropriate evidence.

Auditing the Acquisition and Payment Cycle

This chapter focuses on the audit of the acquisition and payment cycle, which encompasses purchases, accounts payable, and cash disbursements. It describes the typical business functions and related internal controls within this cycle. The chapter details specific audit objectives for assertions such as completeness of liabilities, accuracy of expenses, and proper cutoff for purchases. It outlines various tests of controls (e.g., for purchase requisition approval, invoice matching) and substantive procedures (e.g., search for unrecorded liabilities, vendor statement reconciliations, cutoff tests for purchases and cash disbursements) to ensure the fair presentation of related accounts.

Auditing the Inventory and Warehousing Cycle

This chapter addresses the unique challenges and procedures involved in auditing the inventory and warehousing cycle. It covers the flow of inventory from raw materials to finished goods, including related internal controls over production, costing, and physical custody. Key audit procedures discussed include observing physical inventory counts, performing test counts, evaluating inventory valuation methods (e.g., FIFO, LIFO, weighted-average), and testing inventory cutoff procedures. The chapter also covers substantive procedures for cost of goods sold and related inventory accounts, emphasizing the importance of proper inventory costing and existence.

Auditing the Payroll and Personnel Cycle

This chapter focuses on the audit of the payroll and personnel cycle, which involves transactions related to employee compensation, benefits, and personnel records. It describes the typical functions within this cycle, such as hiring, timekeeping, payroll preparation, and payment, along with related internal controls designed to prevent unauthorized payments or misstatements. The chapter outlines specific audit objectives and procedures for payroll expenses, accrued liabilities (e.g., payroll taxes, vacation pay), and related accounts. This includes tests of controls over payroll processing and substantive procedures like analytical review of payroll expenses and reconciliation of payroll tax forms.

Auditing the Financing and Investing Cycles

This chapter covers the audit of the financing and investing cycles, which involve transactions related to long-term debt, equity accounts (e.g., common stock, retained earnings), investments, and property, plant, and equipment (PPE). It details the internal controls typically found in these cycles, such as authorization for capital expenditures or debt issuance. Specific audit procedures include verifying the existence and valuation of investments and PPE, confirming debt agreements, examining stock transfer records, and reviewing board minutes for authorization of significant transactions. The chapter emphasizes the proper classification and disclosure of these complex accounts.

Completing the Audit and Post-Audit Responsibilities

This chapter focuses on the procedures performed near the end of the audit engagement and subsequent responsibilities. It covers critical steps such as reviewing for contingent liabilities (e.g., lawsuits, warranties), identifying and evaluating subsequent events that occur after the balance sheet date but before the audit report date, and assessing the client's ability to continue as a going concern. Other topics include obtaining a management representation letter, performing a final analytical review, and communicating audit findings and internal control deficiencies to management and the audit committee. It also touches upon the auditor's responsibilities after the audit report has been issued.

Audit Reports

This chapter provides a comprehensive overview of audit reports, explaining the different types of opinions an auditor can issue. It details the standard unmodified (unqualified) audit report and its components. The chapter then discusses modifications to the audit opinion, including qualified opinions (due to scope limitations or GAAP departures that are not pervasive), adverse opinions (for pervasive GAAP departures), and disclaimers of opinion (for pervasive scope limitations or going concern uncertainties). It also covers situations requiring explanatory paragraphs or emphasis-of-matter paragraphs within an unmodified report, such as consistency issues or significant uncertainties.

Other Assurance and Non-Assurance Services

This chapter expands beyond the traditional financial statement audit to cover other services provided by CPAs. It differentiates between assurance services and non-assurance services. Assurance services discussed include reviews of financial statements, which provide limited assurance, and attestation engagements, such as agreed-upon procedures or examinations of internal control over financial reporting. Non-assurance services typically covered include compilations of financial statements, which provide no assurance, and tax or consulting services. The chapter highlights the varying levels of assurance provided by each service and the reporting requirements.

Internal, Operational, and Government Auditing

This chapter explores specialized areas of auditing beyond external financial statement audits. It details the role and responsibilities of internal auditors, including their organizational independence and adherence to the International Standards for the Professional Practice of Internal Auditing. Operational auditing, focused on evaluating efficiency and effectiveness of an organization's operations, is also discussed. Furthermore, the chapter covers government auditing, introducing Government Auditing Standards (the Yellow Book) issued by the GAO, which apply to audits of governmental entities and entities receiving federal awards, often requiring audits of compliance and internal control over compliance.

IT Auditing and Data Analytics

This chapter addresses the impact of information technology (IT) on the audit process. It covers how auditors assess IT risks and controls, including general controls (e.g., access security, program development) and application controls (e.g., input, processing, output controls). The chapter explains how auditors audit in an IT environment, including auditing around the computer and through the computer. A significant focus is placed on the use of computer-assisted audit techniques (CAATs) and data analytics tools to enhance audit efficiency and effectiveness, such as analyzing large datasets for anomalies, trends, and patterns, and performing substantive tests more comprehensively.

Themes

- Professional Skepticism
- Ethical Conduct
- Risk Assessment
- Evidence Gathering
- Regulatory Compliance
- Internal Control

Frequently Asked Questions

What is Auditing & Assurance Services about?

This textbook provides a comprehensive guide to the principles and practices of auditing and assurance services. It covers the entire audit process, from planning and risk assessment to gathering evidence and issuing audit reports, emphasizing professional standards, ethics, and the regulatory environment relevant to the accounting profession.

Is Auditing & Assurance Services worth reading?

Yes, it is highly recommended for accounting students, aspiring auditors, and professionals seeking a thorough understanding or a refresher on auditing concepts and procedures. Its practical approach, integration of current standards, and real-world examples make it an invaluable resource for developing essential auditing skills and knowledge.

How does Auditing & Assurance Services end?

Spoiler: The book concludes by covering the completion phase of an audit, including subsequent events, contingent liabilities, and the issuance of various types of audit reports. It also expands beyond traditional financial statement audits to discuss other assurance and non-assurance services, preparing readers for the diverse roles within the profession.

Who should read Auditing & Assurance Services?

This book is primarily intended for undergraduate and graduate students in accounting programs. It is also beneficial for individuals preparing for professional certification exams like the CPA exam, as well as practicing auditors and financial professionals who wish to deepen their understanding of audit methodologies and assurance principles.

How long does it take to read Auditing & Assurance Services?

Given its comprehensive nature as a textbook, reading "Auditing & Assurance Services" typically takes around 960 minutes (16 hours) for a focused reader. However, students often engage with it over an entire semester, studying specific chapters and sections in depth.