# The Demand for Audit and Other Assurance Services

Chapter 1



#### Sarbanes-Oxley Act

The Act established the Public Company Accounting Oversight Board.

It also requires auditors to attest to management reports on the effectiveness of internal control over financial reporting.



### • • Learning Objective 1

Describe auditing.



#### Nature of Auditing

Auditing is the accumulation and evaluation of evidence about information to determine and report on the degree of correspondence between the information and established criteria.

Auditing should be done by a competent, independent person.



## Information and Established Criteria

To do an audit, there must be information in a verifiable form and some standards (criteria) by which the auditor can evaluate the information.



## Accumulating Evidence and Evaluating Evidence

Evidence is any information used by the auditor to determine whether the information being audited is stated in accordance with the established criteria.



#### Competent, Independent Person

The auditor must be qualified to understand the criteria used and must be *competent* to know the types and amount of evidence to accumulate to reach the proper conclusion after the evidence has been examined.

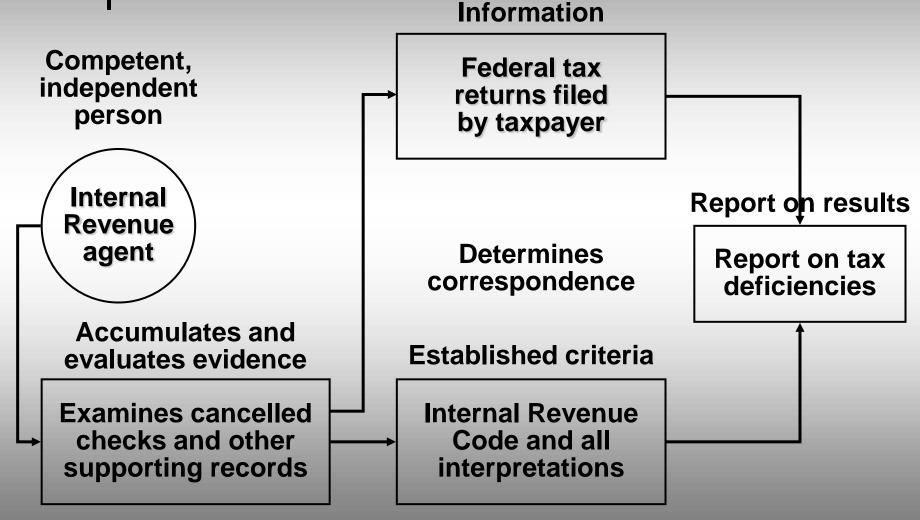
The competence of the individual performing the audit is of little value if he or she is biased in the accumulation and evaluation of evidence.



#### • • Audit Report

The final stage in the auditing process is preparing the Audit Report, which is the communication of the auditor's findings to users.

#### Audit of a Tax Return Example





#### • • Learning Objective 2

Distinguish between auditing and accounting.



## Distinguish Between Auditing and Accounting

**Accounting** is the recording, classifying, and summarizing of economic events for the purpose of providing financial information used in decision making.

Auditing is determining whether recorded information properly reflects the economic events that occurred during the accounting period.



### • • Learning Objective 3

Explain the importance of auditing in reducing information risk.



## Economic Demand for Auditing

Information risk reflects the possibility that the information upon which the business risk decision was made was inaccurate.

Auditing can have a significant effect on information risk.



### • • Learning Objective 4

List the causes of information risk, and explain how this risk may be reduced.



### Causes of Information Risk

- > Remoteness of information
- > Biases and motives of the provider
- > Voluminous data
- > Complex exchange transactions



### • • • Reducing Information Risk

- > User verifies information
- > User shares information risk with management
- > Audited financial statements are provided



#### • • Learning Objective 5

Describe assurance services and distinguish audit services from other assurance and nonassurance services provided by CPAs.



#### Assurance Services

An assurance service is an independent professional service that improves the quality of information for decision makers.

Assurance services can be performed by CPAs or by a variety of other professionals.



#### Attestation Services

An *attestation service* is a type of assurance service in which the CPA firm issues a report about the reliability of an assertion that is the responsibility of another party.



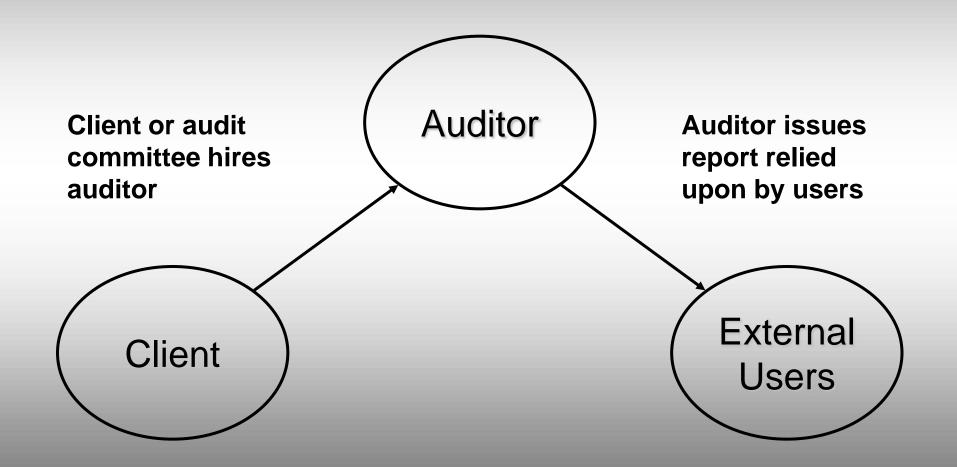
#### • • Attestation Services

#### **Five Categories:**

- 1. Audit of historical financial statements
- 2. Attestation of internal control over financial reporting
- 3. Review of historical financial statements
- 4. Attestation services on information technology
- 5. Other attestation services



## Relationships Among Auditors, Client, and External Users





#### Other Assurance Services

Most of the other assurance services that CPAs provide do not meet the formal definition of attestation services.

The CPA is not required to issue a written report.

The assurance does not have to be about the reliability of another party's assertion about compliance with specified criteria.



#### • • • AICPA Assurance Services

The AICPA formed the Special Committee on Assurance Services (SCAS).



## Attestation Services on Information Technology

WebTrust is an attestation service, and the WebTrust seal is a symbolic representation of the CPA's report on management's assertions about its disclosure of electronic commerce practices.



## Attestation Services on Information Technology

SysTrust is an attest-type engagement to evaluate and test system reliability in areas such as security and data integrity.



## Principles for WebTrust and SysTrust Services

- 1. Online privacy
- 2. Security
- 3. Processing integrity
- 4. Availability
- 5. Confidentiality
- 6. Certification authorities (WebTrust only)



## Nonassurance Services Provided by CPAs

- 1. Accounting and bookkeeping services
- 2. Tax services
- 3. Management consulting services



Controls over and risks related to investments, including policies related to derivatives...

#### involves

assessing the processes in a company's investment practices to identify risks and to determine the effectiveness of those processes.



Mystery shopping...

#### involves

performing anonymous shopping to assess sales personnel dealing with customers and procedures they follow.



Assess risks of accumulation, distribution, and storage of digital information...

#### involves

assessing security risks and related controls over data and other information stored electronically, including the adequacy of backup and off-site storage.



Fraud and illegal acts risk assessment...

#### involves

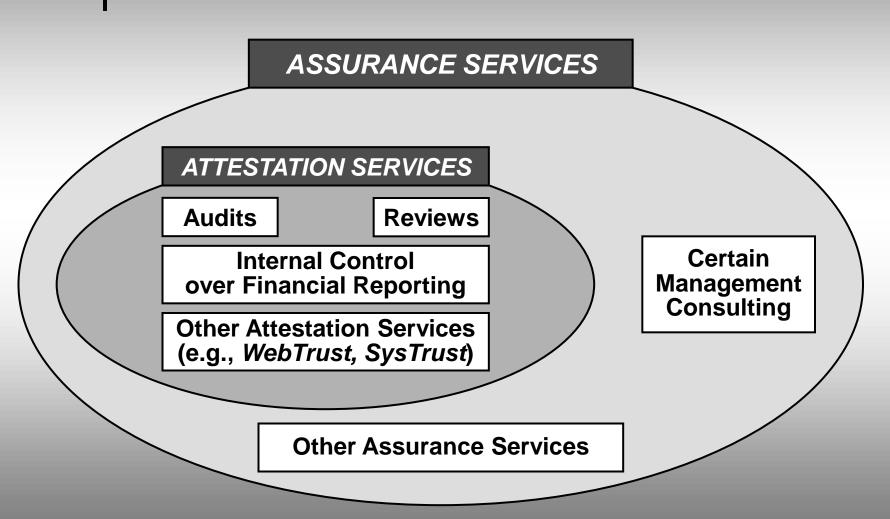
developing fraud risk profiles and assessing the adequacy of company systems and policies in preventing and detecting fraud and illegal acts.



- > Compliance with trading policies and procedures
- > Compliance with entertainment royalty agreements
- > ISO 900 certification
- > Environmental audit

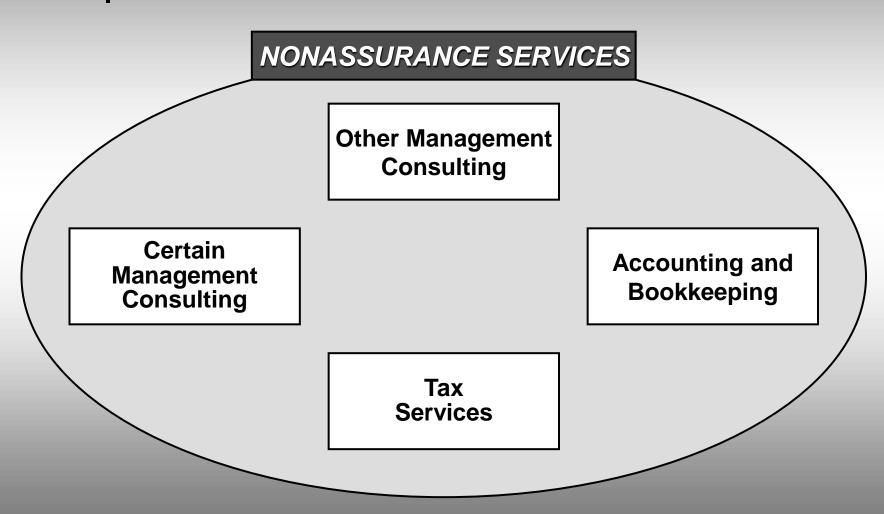


## Assurance, Attestation, and Nonassurance Services





## Assurance, Attestation, and Nonassurance Services





#### • • Learning Objective 6

Differentiate the three main types of audits.



#### Types of Audits

- Operational
- > Compliance
- > Financial Statement



### • • Operational Audit

Example	Evaluate computerized payroll system for efficiency and effectiveness
Information	Number of records processed, costs of the department, and number of errors
Established Criteria	Company standards for efficiency and effectiveness in payroll department
Available Evidence	Error reports, payroll records, and payroll processing costs



#### • • Compliance Audit

Example	Determine whether bank requirements for loan continuation have been met
Information	Company records
Established Criteria	Loan agreement provisions
Available Evidence	Financial statements and calculations by the auditor



## Audit of Historical Financial Statements

Example	Annual audit of Boeing's financial statements
Information	Boeing's financial statements
Established Criteria	Generally accepted accounting principles
Available Evidence	Documents, records, and outside sources of evidence



#### • • Learning Objective 7

Identify the primary types of auditors.



### Types of Auditors

- > Independent certified public accounting firms
- > Governmental general accounting office auditors
- > Internal Revenue agents
- > Internal auditors



### • • Learning Objective 8

Describe the requirements for becoming a CPA.



## Three Requirements for Becoming a CPA

- > Educational requirement
- > Uniform CPA examination requirement
- > Experience requirement



## CPA Examination Sections

- Auditing and Attestation
- > Financial Accounting and Reporting
- > Regulation
- > Business Environments and Concepts

### End of Chapter 1