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OVERALL OBJECTIVES OF THE INDEPENDENT AUDIT

According to the ISA 200 «Overall objectives of the independent auditor and the conduct of an audit in accordance with international standards on auditing», the objective of an audit is to enable the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an identified financial reporting framework. This framework might be International Accounting Standards, or the national standards of a particular country. The phrases used to express the auditor's opinion are that the financial statements «give a true and fair view» or «present fairly in all material respects». These phrases, which are equivalent terms, are used in many countries, including the UK and the US.

The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements.

The financial statements subject to audit are those of the entity, prepared by management of the entity with oversight from those charged with governance. ISAs do not impose responsibilities on management or those charged with governance and do not override laws and regulations that govern their responsibilities. However, an audit in accordance with ISAs is conducted on the premise that management and, where appropriate, those charged with governance have acknowledged certain responsibilities that are fundamental to the conduct of the audit. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.

Financial statements include balance sheets, income statements, statements of changes in financial position (such as cash flow statements), notes and other explanatory material that are identified as being part of the financial statements. What is included in the audited financial statements, and what is excluded, is determined largely by national legislation and accounting standards.

We should distinguish between audits and related services such as reviews, agreed-upon procedures and compilation reports which are dealt with later in this text. Reviews and agreed-upon procedures do not give the same high level of assurance as an audit, and compilation reports do not involve the expression of an «opinion» at all.

It is important that auditors do not certify the financial statements or guarantee that the financial statements are correct; they report that in their opinion they give a «true and fair view», or «present fairly» the financial position. Also, we should distinguish at this stage between external and internal audit. Statutory audits and other engagements described above are all carried out by



auditors external to the company or organization being audited (referred to as the «external auditor»). Internal auditing is generally practiced by auditors actually employed by the company or organization.

An audit in accordance with ISAs is designed to give reasonable assurance that the financial statements are free from material misstatement. However, there are inherent limitations in an audit that can affect the auditor's ability to detect material misstatements. These include the use of sampling, the fact that most audit evidence is persuasive rather than conclusive, and the fact that internal control systems have their own inherent limitations. For these and other reasons, an audit that fails to detect a material misstatement is not necessarily a negligent audit.

The need for an audit centres on the requirements of the users of the accounts, the «stakeholders». The financial statements account annually to the shareholders for the stewardship of the directors and the management. There are also many other outside parties who use the financial statements as a basis for making decisions regarding a company. Bankers, trade and loan creditors as well as potential investors and employees all have an interest in the state of the company's financial affairs. The independent audit requirement fulfils the need to ensure that those financial statements are objective, free from bias and manipulation and relevant to the needs of the users.

There is a general misconception that the purpose of an audit is to detect fraud and taxation errors. Many countries, particularly in Central and Eastern Europe and the former CIS, require a separate audit for taxation purposes. There, the requirement for an audit on the financial statements is a relatively new one as previously there was no distinction between tax accounts and financial accounts, as there were no active capital markets.

So, true and fair is the central underlying concept relating to the audit. The audit opinion relates to the material amounts in the financial statements and the objectives of an audit have also been covered and need to be borne in mind at all times.

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