Approved through
Court of Accounts Decision

No 70, dated October 16, 2006

AUDIT STANDARDS APPLICABLE AT THE STAGE OF AUDIT PROCEDURES

2.1. Audit evidence

The objective of this standard is to provide guidelines on audit evidence characteristics that are to be collected to deliver the audit objectives, as well as procedures that are to be performed to gather the audit evidence.

Guidelines and explanations

Audit evidence shall be gathered and used by controllers to support findings, conclusions and recommendations both within financial and performance audit.

The financial audit findings, conclusions and recommendations shall be based on competent, valid and true audit evidence to be obtained by the controller.

Competent audit evidence is credible information and data.

Valid audit evidence is the information that supports documentarily audit findings.

True audit evidence is the information compliant with the real situation.

The evidence obtained by the controller within financial audit should meet the following objectives:

a) **existence:** an asset or liability exists at a given moment;
b) **rights and liabilities**: an asset or liability belongs to the entity on a given date;
c) **occurrence:** a transaction or event happened during a given period and belongs to the entity;
d) **completeness:** all assets, liabilities, transactions or events have been recorded and all items submitted;
e) **valuation:** an asset or liability is recorded at a correct accounting value;
f) **measurement:** a transaction or event is recorded at its correct value;
g) **presentation:** an element is presented, classified and described according to the applicable reporting framework (for example, relevant legislation and applicable accounting standards).

While in financial audit the reviews performed by controllers shall disclose that financial operations are appropriate or incorrect, legal or illegal, etc., in performance audit, the criteria used for findings and conclusions on economy, efficiency and effectiveness shall be based on ***competent***, ***relevant*** and ***reasonable*** evidence.

Audit evidence is ***competent*** when it is quantitatively sufficient, and qualitatively appropriate, as well as impartial, so that it provides reliability and assurance.

Audit evidence is ***relevant***, if it is based on data and information related to audit objectives and criteria.

Audit evidence is ***reasonable***, if collection of data and information was carried out efficiently and at low costs.

Audit evidence ***credibility*** is influenced by its source, which can be internal or external, by its nature, that can be visual, documentary or oral, as well as by the circumstances in which it was obtained. Though audit evidence credibility depends on certain circumstances in which it was obtained, when assessing audit evidence credibility the following generalizations shall be considered:

- **external audit evidence (information obtained from third parties) is more credible than internal audit evidence;**
- **internal audit evidence is more credible when accounting and internal control systems operate efficiently;**
- **documentary audit evidence is more credible than verbal audit evidence;**
- **audit evidence obtained by controller is more credible than that obtained indirectly;**
- **original papers are more credible than photocopied papers; when original papers are photocopied by controllers, they have to record the source and date when they were photocopied;**
- **audit evidence is more convincing, if other evidence or that obtained from different sources is not contradicting;**
- **if audit evidence obtained from one source does not correspond to the evidence obtained from another source, the controller shall perform additional procedures to remove contradiction;**
- **if there are considerable doubts about the qualitative and significant aspects of financial reports, the controller shall obtain sufficient appropriate audit evidence to expel such doubts. If such evidence can not be obtained, the controller shall express a qualified opinion or disclaimer of opinion.**

Audit evidence is the information collected by the controller from primary documents and accounting recordings underlying the financial statements presented by the audited entity or from other sources by performing ***tests of control*** and ***substantive procedures***.

Tests of control are the tests applied by the controller to obtain audit evidence on the effective operation of audited entity’s accounting and internal control systems.

Substantive procedures are the tests applied by the controller to identify material errors in audited entity's financial statements. ***Analytical procedures*** and ***tests of detail*** belong to substantive procedures.

Findings, conclusions and recommendations shall be based on audit evidence which controllers obtain after applying ***audit techniques*** and ***procedures***.

The Director of the department, head of the division and the board member of the Court of Accounts, who manage the audit shall make sure that the techniques used by controllers are sufficient and appropriate to detect any quantitatively significant errors and irregularities, and in performance audit – to discover the qualitative ones.

The selection of the best techniques for obtaining and analyzing audit evidence shall be performed by considering controller's professionalism, logic and competence. These in turn will determine the need to deepen or not certain aspects of audit, the time spent on reviews, as well as the cost for gathering audit evidence.

Audit procedures shall include the following stages:

- ***review*** – examination of recordings, documents and material assets. There are three main types of documentary audit evidence with different credibility degrees for controller:
  a) documentary audit evidence, produced and submitted by third parties;
  b) documentary audit evidence, produced and submitted by the audited entity;
  c) documentary audit evidence, produced by third parties and submitted by the audited entity.
- ***observation*** – examination and witnessing of procedures or processes which do not require documentation or which are performed by other persons, such as participation in stock–taking conducted by audited entity's staff;
- ***investigation and confirmation*** – collecting information from competent sources within the entity (management, staff) or outside the entity, such as banks, suppliers, etc. Investigations will vary from formal, written, addressed to third parties as required, up to informal, verbal, addressed to entity's staff / management. The goal of these notifications implies that the answers to inquiries will provide the controller with information he /she lacked or with justifying audit evidence. Confirmation is the reply to the inquiry for attesting accounting information;
- ***computation*** – checking the accuracy of accounting entries in primary documents and books of accounts or independent calculations.

Methods and techniques for collecting audit evidence within performance audit shall be specific, having the goal to disclose facts (findings), identify cause-effect relationships, test the rationales and suggest improvement options.

The most common methods and techniques for collecting audit evidence in performance audit are the following: *inspection of papers, analysis of some reports, organization of debate groups, questionnaires, interviews, direct observation*.

Within performance audit, the audit evidence (data, information) shall be used mainly to establish if audited entity's manager and staff acted according to the operational principles established through adopted policies and standards and used the resources economically, efficiently and effectively.

By its nature, *the following types of audit evidence may be distinguished:*

a) *physical audit evidence* **– obtained through direct observation of events /phenomena and activities /actions of staff in the shape of pictures, diagrams, graphic maps and other presentations;**

b) *verbal audit evidence* **– obtained in the shape of answers to interviews, surveys, etc.;**

c) *documentary audit evidence* **– obtained exclusively from written or electronic papers;**

d) *analytical audit evidence* **– obtained on the basis of examination, analysis and interpretation of data resulting from actions relating to a program implementation or an activity performed by the audited entity.**

The evidence in performance audit shall be obtained by:

a) ***paying some visits to audited entity's headquarters*** **to examine the papers and interview officials;**

b) ***sending /remitting*** **intercessions or** ***addressing some questionnaires*** **that include questions relating to audited topic;**

c) ***withdrawing and examining a representative sample from a certain population.***

Within performance audit, the audit evidence shall be analyzed and interpreted by applying the following methods:

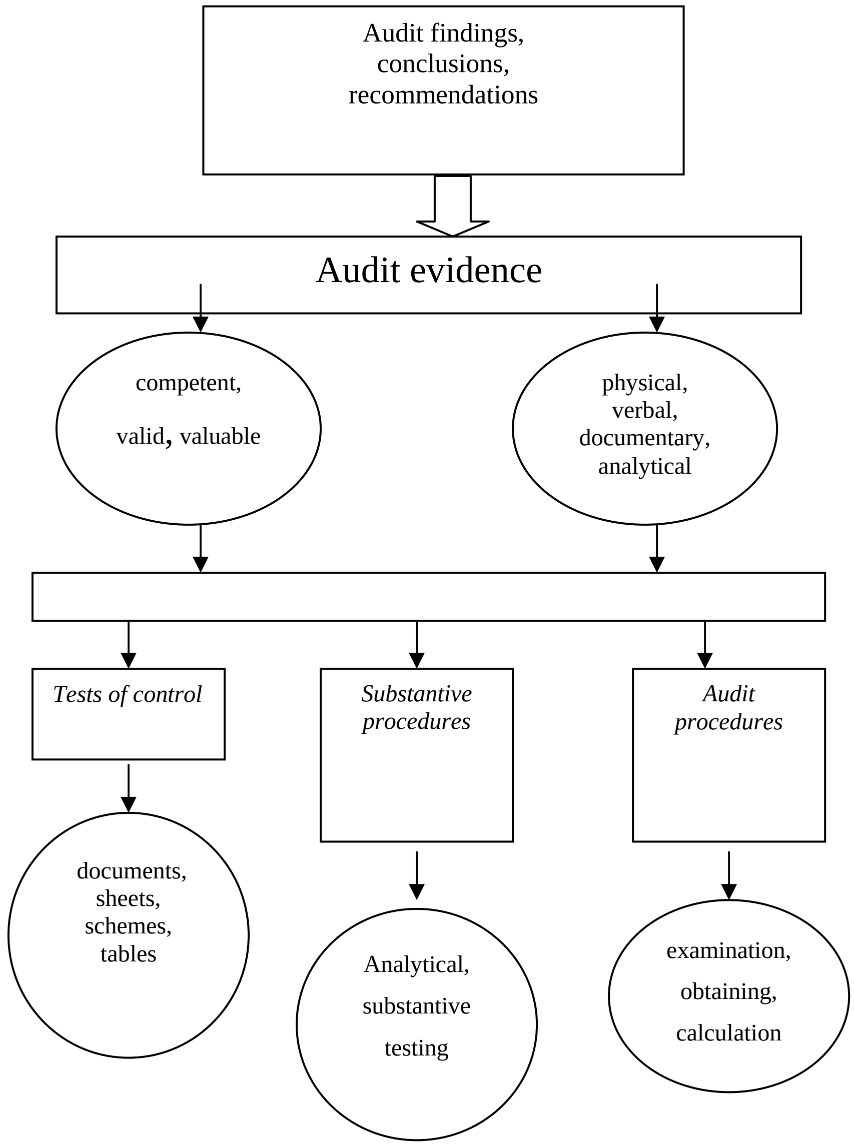
- **filling in some tables and designing of some graphics to summarize quantitative data and information;**
- **calculation of performance indicators (unit value, per capita income);**
- **laying–out by diagrams with further description and analysis;**
- **filling in tables by comparing criteria with conditions;**
- **analysis of a sample of events to highlight positive and negative examples.**

Controllers should know well enough specific techniques for collecting audit evidence: inspection, observation, investigation, confirmation and calculation.

- *Inspection* **consists in examination of records and documents.**
- *Observation* **consists in witnessing a process or procedure performed by other persons.**
- *Investigation* **consists in obtaining information (available) from persons within or outside the audited entity.**
- *Confirmation* **consists in the answer to an inquiry to support the information from the accounting records.**
- *Calculation* **means the verification of arithmetical accuracy of documents and accounting records.**

The audit evidence underlying audit findings, conclusions and recommendations and the methods for obtaining them are presented schematically below.

Diagram



2.2. Analytical procedures

The goal of this standard is to establish the guidelines on analytical procedures, reasons for and importance of their use within audit.

Guidelines and explanations

Controllers shall use analytical procedures at planning stage, audit procedures and audit reporting.

Analytical procedures shall imply analysis by controller of figures, indicators, material items, investigation of irregularities and changes in the techniques of entities' activities that generate instability in the results and scheduled /forecast values.

Controller shall perform analytical procedures to ensure that disparities are reasonable and the explanations provided justify irregularities and changes occurred in entity's financial-economic position.

Analytical procedures shall provide for comparison of entity's financial information for the current period with:

- comparable analytical information from previous periods;
- forecast indicators, such as budgets;
- average indicators of the area and other entities conducting similar activities and competence. Such a comparison shall be carried out by the controller within the audit of a document, line and departmental state programs of the local public administration, etc.

Analytical procedures shall also include the examination of interconnections:

- between financial indicators (or of any other non-financial information), which, according to controller's opinion, should correspond to the trends of previous years;
- between financial and non-financial relevant information (for example, the relationship between pay-roll expenditures and their average in-house staff number).

Various methods could be used for performing the above mentioned procedures: from simple comparisons to complex analyses by applying advanced statistical methods. Controller's choice regarding the procedures, methods and their application degree shall depend on controller's professional qualifications.

Analytical procedures shall be performed:

a) as substantive procedures, when their use in mitigating detection risk of qualitative aspects of financial statements can be more efficient than testing;
b) during walk-through tests of financial statements at the final stage of audit.

Controller's reliance on the result of analytical procedures shall depend on the following factors:

a) materiality of reviewed indicators, for example, if account balances of stock-in-trade and tangibles are significant, then in expressing conclusions, the controller shall not rely only on analytical procedures;
b) other audit procedures aimed at achieving the same audit objectives;
c) accuracy with which results of analytical procedures can be forecast;
d) assessment of inherent and control risks.

If during analytical procedures significant irregularities and /or modifications that deviate from forecast indicators are identified, the controller should carry out an investigation and obtain appropriate explanations and supportive evidence.

Investigation of irregularities /modifications shall include management inquiry, followed by:

- analysis of objective achievement level to determine if the established objectives have been delivered, as well as to identify the factors that led to quicker or poorer attainment of objectives;
- cost-benefit analysis, aimed at reviewing if the incomes of an entity, program or activity exceeded the costs and do not exceed the planned level;
- cost-efficiency analysis focused on identifying the most advantageous means of achieving certain objectives, under a maximum level of appropriated expenditures.

2.3. Documentation in audit activity

The objective of this standard is to provide guidelines on the need and importance of working papers compiled by and for controller or obtained by him /her within the audit.

Guidelines and explanations

The controller shall be aware of the fact that the presentation and content of working papers reflect the degree of his /her competence, experience and knowledge. The controller shall draft the working papers so that they are sufficiently detailed and complete to ensure overall understanding of the works performed by controller.

Appropriate documentation regarding audit activity is necessary:

- to confirm and support controller's judgment and reports;
- to increase audit efficiency and effectiveness;
- to establish a sound source of information when concluding reports;
- to serve as audit evidence in compliance with audit standards;
- to ease audit planning and conduct;
- to contribute to professional preparation of audits;
- to check permanently if planned activity was performed adequately;
- to provide audit evidence that will serve as documentary materials for further activities.

Controller should document audit evidence establishing audit areas according to legal competence, audit scope, activity to be carried out and audit conclusions.

Contents, drafting and presentation of working papers should correspond to the following requirements:

a) to be complete and processed accurately in order to provide an appropriate basis for findings and recommendations;
b) to be clear, logical, without requiring additional explanations;
c) to be reader-friendly, without corrections and further additions.

As a rule, the working papers shall include:

- information about entity's legal organizational form and organizational structure;

- extracts or copies of entity's Deeds of Incorporation, other legal papers, agreements, contracts, minutes, etc.;
- information (publications, statistical data, etc.) regarding the field /area, economic and legal environment in which the entity operates;
- information about the planning process, economic indicators;
- evidence on the study and application of accounting and internal control systems (descriptions, questionnaires, document movement cycles, etc.);
- information about inherent and control risk assessment, as well as their further modifications;
- information confirming controller's examination of internal audit activity and stated conclusions;
- analysis of economic transactions and bookkeeping account balances;
- analysis of material indicators and trends in entity's activity (analytical procedures);
- copies of intercessions to experts and other third parties;
- intercessions, notes and other written statements received from entity's management;
- controller's conclusions on audit significant aspects;
- copies of financial statements and controller's report.

Working papers shall include reference to the source of information included therein and an identification number.

Working papers may be drafted on paper, technical record or other information holder.

Working papers shall be the property of the Court of Accounts during audit conduct.

The information from the documents shall be confidential and may not be subject to disclosure by controller to third parties. The latter, including tax bodies and other authorities shall not have the right to require from the controller the working papers or their copies, except for the cases stipulated by legislation.

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- **The audit standards shall be approved by the Court of Accounts and published in a special booklet.**

- **These audit standards shall be meant for internal use, and shall be completed and amended depending on the requirements that may occur in a year after their application in practice.**

Glossary

- **Performance audit** – independent and objective review or assessment of how efficiently and effectively a program or activity in an entity's area operates by observing the economy principle.
- **Financial audit** – examination whether the financial statements are complete and accurate, and whether transactions are legal and regular.
- **Audit of financial statements** – independent review of entity's financial statements, aimed at expressing controller's opinion whether financial statements are prepared, in all material aspects, in compliance with the requirements established in relation to these statements.
- **Population** - the set /group of data from which the controller shall select a sample and on which the auditor shall base his /her conclusions.
- **Internal control** - control established by entity's management to offer reasonable assurance on the efficiency and effectiveness of operations, reliability of financial information, and compliance with legal framework.
- **Key controls** – a set of controls aimed at mitigating audit risks.
- **Audit sampling** – performance of audit procedures to less than 100 per cent of account balance items or class of transactions, so that all sampling items have the same chance of being selected.
- **Materiality** - shows the maximum tolerable level of acceptable error enabling to decide whether the accounts are correct or incorrect.
- **Audit program** – controller's working paper setting out the nature, extent, timing and volume of planned audit procedures, necessary to implement the General Audit Plan.
- **Substantive procedures** – tests carried out to obtain audit evidence for identification of material misstatements in financial statements.
- **Audit risk** - the risk that the auditor will express an inappropriate audit opinion when entity's financial statements are materially misstated.

- **Inherent risk** – tendency of an account balance or certain class of transactions to be misstated.
- **Control risk -** the risk that a misstatement of an account balance or class of transactions, that could be material, individually or aggregated with misstatements from other account balances or classes of transactions will not be prevented or detected and corrected on a timely basis by the accounting and internal control systems.
- **Detection risk** - the risk that the substantive procedures will not detect a misstatement in an account balance or class of transactions that could be material individually or when aggregated with misstatements in other account balances or classes of transactions.
- **Sampling risk** - the likelihood that controller's conclusion, based on a sample, may be different from the conclusion that could be reached if the entire population had been subject to the same audit procedure.
- **Non-sampling risk** – the risk that arises as a result of the impact of factors which determine the controller to express an erroneous conclusion for any reason not related to the size of the sample.
- **Audit standards** – the document that offers minimum guidance to the controller for defining audit stages and procedures that will enable the attainment of the objective concerned.
- **Tests of control** – performance of tests to obtain audit evidence on the reasonable nature of structure and efficiency of the operation of accounting and internal control systems.

Glossary

- **Materiality** – qualitative nature of information. Information shall be regarded as material if its omission or misstatement can influence the economic decisions taken by users based on financial results. Materiality level shall depend on indicator or error size, assessed in certain circumstances.
- **Audit evidence credibility** – certainty about their power that provides the possibility for their use.
- **Working papers** – controller's records about planning, nature, timing and extent of performed audit procedures, results of these procedures, as well as the conclusions drawn on the basis of obtained audit evidence.
- **Comparatives** – the information disclosed within financial statements relating to previous reporting period /s and presented for comparison in the shape of corresponding data; financial statements; research financial information; interim financial information or statements.
- **Audit evidence** – data and information that support audit opinions, conclusions and reports.
- **Analytical procedures** – procedures by which controller uses financial or non-financial data to forecast a figure in the financial statements.
- **Audit procedures** - ways by which the controller obtains audit evidence.
- **Substantive tests** – tests performed by controller on some individual transactions.