

MODERN MAINSTREAM IN AUDIT: RISKS AND THEIR ASSESSMENT

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Introduction. The concept of audit risk is one of the most important in audit activities, since the level of audit risk is necessary to plan the audit and determine audit procedures in accordance with the assessed risk.

According to the IAASB Glossary of Terms [5], audit risk is defined as follows ‘The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of material misstatement and detection risk. Audit risk is basically to the audit process because auditors cannot and do not attempt to check all transactions.

Overview of recent researches and publications. Audit risk based model and implementation of its concept of auditing activity is an effective method of sustainable economic development. A significant contribution to the development of conceptual approaches and paradigm of new auditing mainstream is highlighted in the scientific works by such scientists as: I. Dmytrenko, T. Kamenska, K. Nazarova, O. Petrik, N. Proskurina, O. Rubitel et al.

The purpose of the article is to determine the essence, principles and mechanisms of functioning of the audit risk based model, which is recognized as one of the vectors for the implementation of the concept of sustainable development both as auditing activities and clients developing.

Basic material and results. Under the influence of the current challenges of the world economy, traditional forms of audit are actively transforming. The increased attention and widespread practice of implementing the principles of the risk based audit is explained by the active involvement of not only governments and legal entities of economic relations, but also ordinary business entities in these processes.

The vast number of transactions in a statement of comprehensive income and a statement of financial position could not be check efficiency. To minimize the chance of giving an inappropriate audit opinion auditors should use risk based approach toward auditing. Auditors should direct audit work to the key risks, where it is more likely that errors in transactions and balances will lead to a material misstatement in the financial statements

Audit risk is the actions that the auditor must take depending on the freedom of choice available to him and it is critical to the entire audit process.

During the audit, the auditor faces three types of risks: accounting, control and audit procedures.

So, the audit risk is based on the estimation:

- the risk of inefficiency of the accounting system, which is maintained by the client;
- the risk of ineffectiveness of the client's internal control system;
- the risk of non-detection of client errors by auditors when performing audit procedures.

The first component of audit risk (risk of material misstatement) is associated with the peculiarities of the functioning of the client enterprise, its accounting system and internal control. In other words, the risk of material misstatement is the likelihood of material misstatements in the financial statements before the audit, but after the control procedures introduced by the entity have been implemented. These risks cannot be influenced by the auditor in any way, since they exist independently of the audit of the financial statements. Auditor can only assess the level of these risks, helps to better understand them, but he is not able to reduce

or change them. The inherent risk is considered to be higher if a high degree of judgment and assessment is required or if the entity's operations are very complex.

Control risk is a function of the effectiveness of the internal control system, implemented and maintained by management in order to address the identified risks, relevant to financial reporting, that threaten the achievement of the objectives of the enterprise. That is, businesses must have adequate internal controls to prevent and detect fraud and error.

The difficulty of estimating control risk for the auditor is due to the fact that most enterprises do not have a formalized system of internal control or neglect to document its results. The risk of non-identification is a function of the effectiveness of the audit procedure as it relates to the nature, timing and extent of the procedures determined by the auditor to reduce audit risk to an acceptably low level.

The auditor's risk needs to be considered in several ways, namely:

- 1) risk as an economic category from the standpoint of business results (the likelihood or threat of the auditor losing his reputation, not receiving planned income, or unexpected expenses);
- 2) risk is a probabilistic category from the standpoint of the occurrence of any event, will lead to the auditor expressing a positive opinion about "bad" reporting or expressing a negative opinion about "good" reporting (make incorrect conclusions about the actual state of affairs).

"Audit risk" is the risk that an auditor may give an inappropriate audit opinion on financial statements that are materially misstated. To reduce the audit risk to an acceptably low level means the auditor needs to be more than certain that the financial statements are not materially misstated. This is reiterated by ISA 200, which states, "The auditor should plan and perform the audit to reduce audit risk to an acceptably low level that is consistent with the objective of an audit." "Inherent Risk" as per ISA 400 is "the susceptibility of an account balance or class of transactions to misstatements that could be material, individually or when aggregated with misstatements in other balances or classes, assuming that there are no related internal controls" [1].

According to risk based approach, auditor could plan and provide necessary procedures to identify and recognize fraud or error in an audit of financial statements. The Standard that regulate this issue is ISA 240 "The auditor's responsibilities relating to fraud in an audit of financial statements"[1]. Let's to analyze compliance requirements according to ISA 240 more detailed (in part of risk-based approach and related activities to plan audit procedures). Para 32 ISA 240 requires auditors to design and perform audit procedures:

- Test the appropriateness of journal entries in general ledger and other adjustments made in the preparation of the accounts.
- Review accounting estimates for bias and consider whether this represents a risk of material misstatement due to fraud.
- For significant transactions outside the normal course of business, or that appear unusual (given our understanding of entity/environment/other information noted during audit), we need to evaluate whether the business rationale (or lack) suggests they are there to conceal misappropriation of assets/fraudulent financial reporting.

Based on this audit Audit Strategy plan could cover follow procedures (Fig. 1).

The auditor evaluates the risks in order to determine the questions regarding:

- resources required for specific audit areas, including the use of personnel with relevant experience in high-risk areas, or the use of experts on complex issues;
- the amount of resources required to be used at specific audit sites (to oversee the inventory process, to check the work of other auditors in the case of a group audit, to check high-risk areas, etc.);
- the timing of resource utilization at intermediate stages of the audit or at key closing dates;
- to manage and oversee such resources (conduct briefings and audit team meetings, conduct peer and performance review by partner and leader, conduct quality assurance checks on the engagement, etc.).

The estimation of the risks of material misstatement affects the appropriateness of any sampling method for testing and the size of the audit sample. The identified risks of material misstatement are one of the factors considered by the auditor when formulating requests for external confirmation.

In audit practice, there is still no consensus on the appropriateness of approach to estimating audit risk, so the right to choose remains by the auditor. In any case, it is more important for the auditor to carry out an appropriate risk assessment than the approaches by which such an estimation is carried out. But in any case, the auditor should not neglect the following rules for assessing audit risk:

- you cannot fully rely on the efficiency of the business and the client's accounting system, that is, assume the absence of inherent risk; you cannot fully rely on the efficiency of the client's internal control system;
- any situation should be allowed in which there is a high probability of revealing material misstatements.

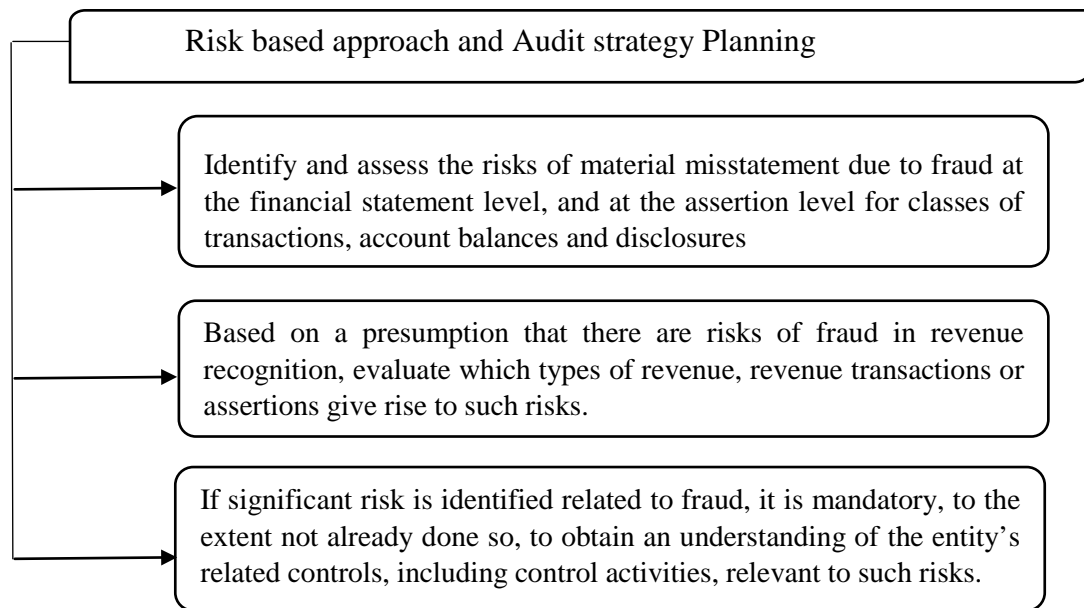


Fig. 1. Identification and Assessment of the Risks of Material Misstatement Due to Fraud

**Complied according to the [1,3,6]*

The main problem in assessing audit risk and its components is subjectivity, therefore it is advisable to develop a methodology for its assessment that can solve this problem. It is rather difficult to level the subjectivity factor, but it is possible by developing step-by-step actions of the auditor to assess risks.

In accordance with ISA 315 (Revised), “Identifying and Assessing the Risks of Material Misstatement Through Understanding the Business Entity and Its Environment” (hereinafter – ISA 315), risk assessment procedures are audit procedures that are performed to [6]:

- 1) gaining an understanding of the enterprise and its environment, including the enterprise's internal control system;
- 2) identifying and determining the risks of material misstatement, whether due to fraud or error, at the financial reporting and assertion levels.

According to ISA 240, the auditor's responses to the assessed risks of material misstatement due to fraud could be (Fig. 2).

As part of gaining an understanding of the risk estimation process, the auditor needs to ensure that the enterprise:

- business risks are identified that are directly related to the objectives of preparing the financial statements;
- an estimation of the probability of their occurrence is carried out;
- their influence (consequences) is assessed;
- decisions are made aimed at their elimination (reduction);
- the risk management process is constantly monitored and adjusted if necessary.

The list of procedures to be performed by the auditor is not exhaustive and depends on the auditor's professional judgment. That is why, in order to gain knowledge about the business of the enterprise, the auditor needs to decide what information will be relevant and useful to achieve the set goal in the process of performing the audit engagement. In practice, auditors mainly use only financial information. This ultimately leads to unreasonable intermediate conclusions regarding the financial activities of the enterprise, since focusing on only one type of information source causes the risk of losing certain important characteristics of the audited object.

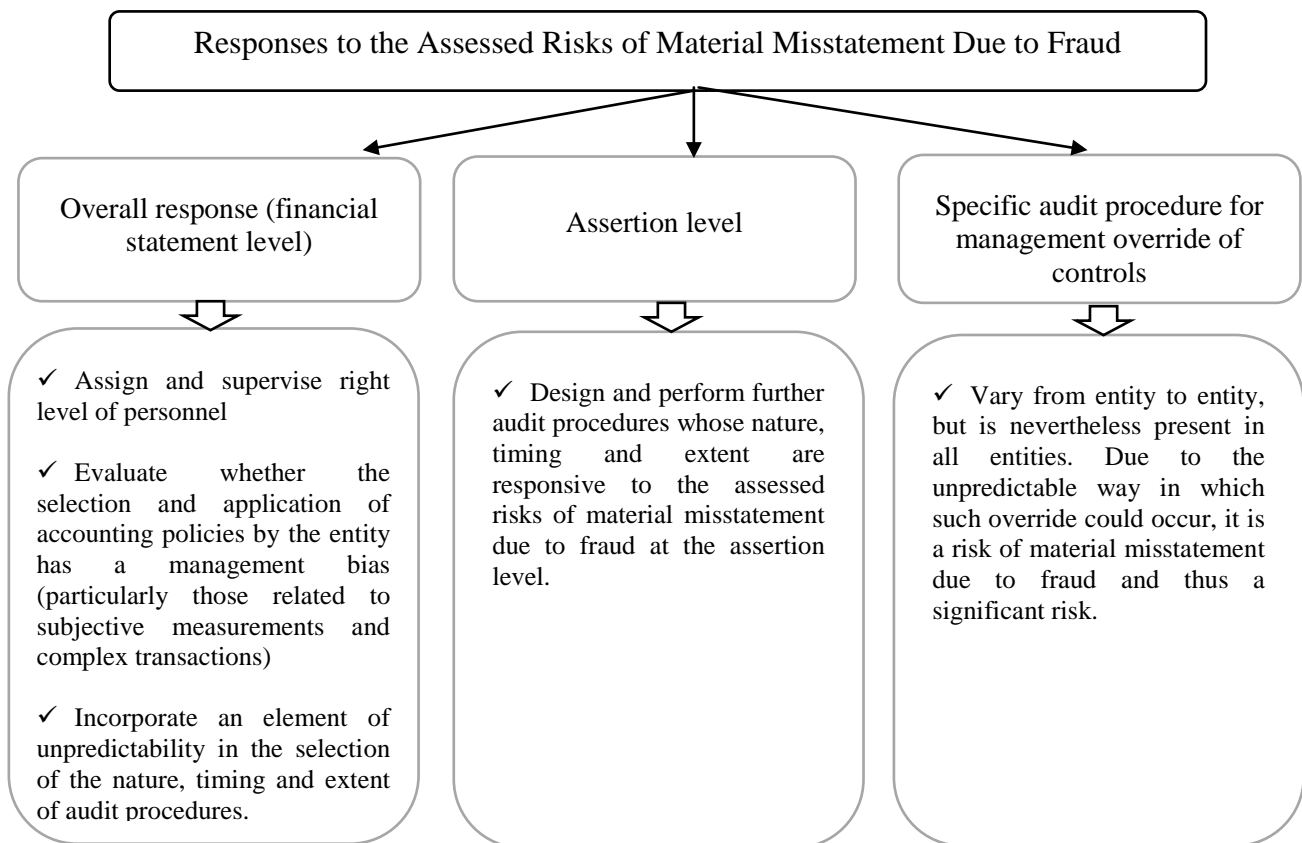


Fig. 2. Responses to the Assessed Risks of Material Misstatement Due to Fraud

**Complied according to the [1,3,6]*

The specific nature of the audit activity, which is associated with the receipt of a large amount of information, its systematization, analysis, the formation of intermediate conclusions, requires the use of professional judgment at all stages of the audit, determines the use of heuristic methods for analyzing information. But the use of such methods can carry the latent threat of falling into "cognitive traps" – errors of the auditor's judgment, which can significantly affect both the interim conclusions of the auditor and the final judgment in the process of forming the audit opinions on the financial statements. Cognitive traps can occur at any stage of the audit.

Investigation of the role of enterprise business knowledge in the audit process will provide an opportunity for a more thorough approach to collecting quality information about a business entity, analyzing it and making informed decisions to achieve this goal, will reduce the risks of errors in the auditor's judgment, the wrong choice of resources for verification, will contribute to the solution of both theoretical and practical problems in planning the audit, conducting the actual review of the assessment of audit evidence and in forming the auditor's opinion.

Conclusions. Knowledge of the business of the enterprise is a prerequisite for ensuring audit quality. The process of studying a business is long and laborious, since it includes not only obtaining information from various sources, but also its systematization and subsequent analysis in order to make appropriate decisions. A proper understanding of the nature of the enterprise is essential in preventing the occurrence of errors in the auditor's judgment.

The lack of clarity in the construction of the risk system and the corresponding estimation methods leads to a violation of the audit methodology, even if the process is formalized.

As a result we can see that there are three main benefits from planning audits: it helps the auditor obtain sufficient appropriate evidence for the circumstances, helps keep audit costs at a reasonable level, and helps avoid misunderstandings with the client.

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Поддубна Наталія Миколаївна, кандидат економічних наук. Київський національний торговельно-економічний університет. **Сучасний мейнстрим в аудиті: ризики та їх оцінювання.** Вплив економічної кризи, непередбачуваної епідеміологічної ситуації у світі на діяльність суб'єктів господарювання є значним та всеосяжним. Тому традиційні підходи до організації аудиторської перевірки (тотального дослідження операцій та первинних документів) довели свою неефективність. Аудиторська спільнота перебуває в постійному пошуку ефективних і прогресивних підходів до планування та організації роботи. У такому випадку ризики є тим головним критерієм, на якому аудитор першочергово фокусує свою увагу. Досліджено процедури ідентифікації, класифікації й оцінювання ризиків. Установлено, що у сучасному світі, сповненому невизначеностей, фундаментальним фактором успіху будь-якого суб'єкта господарювання в різних сферах економіки є управління ризиками. Побудова аудиторської роботи на основі оцінювання ризиків – це хороший шанс і актуальний спосіб зрозуміти різноманітні загрози, з якими стикається організація. Розроблено рекомендації, покликані допомогти отримати раціональне, прагматичне та усвідомлене розуміння про існуючі ризики суб'єкта господарювання.

Ключові слова: аудит, ризик-орієнтований підхід, властивий ризик, ризик контролю, ризик невиявлення.

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Poddubna Natalia, Ph.D (Economics). Kyiv National University of Trade and Economics. **Modern Mainstream in Audit: Risks and Their Assessment.** Impact of the current economic, financial crisis and the coronavirus pandemic on the business activities of companies are very huge and unpredictable. The traditional audit in the form of a total verification of primary documents has proved ineffective. The auditor's world is still grappling with how to ensure the most effective approach to organize their work. Risks are the main vector to which the auditor should pay attention. Risk identification, classification and assessment procedures are investigated in the article. Author has expressed opinion that risk management is fundamental to the success of organizations in every business sector. This is the complex world, full of uncertainty, so whatever its size, it must manage risk. Risk-based audit and assessment is a good chance and a modern way of understanding different threats that an organization faces. Recommendations on a new auditors' approach that should help get a rational and pragmatic view of risk are developed.

Keywords: audit; risk-based approach; audit risk; inherent risk; control risk; detection risk.