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Improving the methodology for completing audits in accordance with international auditing standards

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Abstract

The article examines issues of improving the methodology for completing audits in accordance with international auditing standards. Within the framework of the research, the issues of auditing the main forms of reporting prepared in accordance with International Financial Reporting Standards - the statement of financial position, the income statement and the cash flow statement - were studied in detail. The author analyzed various methods of presenting information in financial statements, classifying assets and liabilities, and grouping expenses.

Keywords: Audit; Financial statements; Audit opinion; Financial position; Profit and loss; Cash flows; International standards

1. Introduction

In modern socio-economic conditions, international market participants are obliged to comply with uniform rules for presenting financial statements. This necessitates the preparation of financial statements in accordance with international standards and their proper auditing.

International Financial Reporting Standards do not require the use of special templates for reporting forms, but establish compliance with certain principles of data presentation and classification. The organization can choose the forms of financial statements itself, but the presentation and classification of items in the financial statements must be the same in each period. The criteria for selecting and applying accounting policies are set out in IFRS (IAS) 8 «Accounting Policies, Changes in Accounting Estimates and Errors».

Financial statement audit is a type of examination, based on the results of which it is possible to determine the correctness of forming and maintaining accounting documents of the entity being inspected. The main purpose of financial statement audit is to express in writing the opinions of qualified employees about the completeness, reliability and legality of the information being examined.

Examining financial statements, that is, auditing, is usually the main revenue item of auditing organizations, and in practice, audit activity usually refers to exactly this type of financial statement examination. The purpose of financial statement audit is to provide the auditor with the opportunity to express an opinion on whether the financial statements have been prepared in all material respects in accordance with established principles of financial reporting.

The purpose of this research is to improve the methodology for examining the main forms of financial statements in the process of completing audits in accordance with international auditing standards and to develop practical recommendations.

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2. Literature review

There is extensive literature on the theory and practice of financial statement audit. Financial statement audit is a comprehensive examination of an organization's accounting statements, conducted to assess data reliability and identify errors in its completion. The concept of reliability expresses the degree of accuracy of information shown in financial statements and allows users to draw correct conclusions about the results of economic activity, financial and property position of the audited entity, and to make informed decisions based on these conclusions.

A.Kh. Kurmanova studied issues of international practice in preparing financial results statements and analyzed differences between national and international standards. Her research focused on comparing various methods of reflecting financial results and identifying optimal approaches.

O.A. Ovchinnikova and N.V. Parushina investigated issues of managing accounts receivable and payable. Their works detail practical aspects of applying discounts and mutual settlements. These issues are important when auditing financial statements.

E.V. Kireeva and O.A. Ovchinnikova compared problems of forming financial results statements in Russian and international practice. Their analysis aimed to identify the main differences between the two systems and indicate ways to bring them closer together.

The theoretical and legal foundations of conducting external audit examinations have been interpreted differently by various economists. In particular, economist R.D. Dusmuratov divided the system of regulatory regulation of audit activities in the Republic of Uzbekistan and its elements into the following three levels:

- The Law of the Republic of Uzbekistan «On Audit Activities»; Resolution No. 365 of the Cabinet of Ministers of the Republic of Uzbekistan «On Improving Audit Activities and Increasing the Importance of Audit Examinations».
- National standards of audit activities; methodological instructions, recommendations for conducting audit examinations, etc.
- Collection of permanent documents of the audit organization, audit examination plan and program, expert documents, etc.
- Economist V.P. Klimovich divides regulatory documents regulating audit activities into the following four levels:

    - Laws and Presidential decrees.
    - Cabinet of Ministers resolutions, ministry instructions and regulations.
    - Standards of audit activities.
    - Internal audit standards.

Economist Kh.N. Musaev divides regulatory documents forming the legal foundations of audit into several types in the following order: regulatory documents related to organizing audit; regulatory documents related to conducting audit; regulatory and legal documents aimed at generalizing and formalizing audit results; regulatory documents related to training and retraining auditors.

IFRS (IAS) 1 «Presentation of Financial Statements» standard establishes the minimum list of assets, liabilities and equity that should be reflected in the statement of financial position. The standard determines the procedure for grouping assets and liabilities items, the procedure for dividing assets and liabilities into short-term and long-term parts, and the minimum additional information that should be announced in the statement of financial position or in related notes.

IFRS (IAS) 7 «Cash Flow Statement» standard discloses requirements for information about cash and cash equivalents, classification of cash flows by type of activity. The standard requires classification of cash flows by operating, investing and financing activities.

IFRS (IAS) 8 «Accounting Policies, Changes in Accounting Estimates and Errors» standard establishes the procedure for selecting and applying accounting policies, changing accounting estimates and correcting errors. This standard plays an important role in ensuring comparability of financial statements.

3. Research methodology

A multifaceted methodological approach was used in the research. Through the theoretical analysis method, scientific literature on international financial reporting standards, legislative documents and regulatory acts were studied. Using the comparative analysis method, the interrelation of national and international standards, their similar and different aspects were identified.

Based on a systematic approach, all stages and factors of implementing IFRS in the Republic of Uzbekistan were analyzed comprehensively. For practical research, the case study method was applied, and the financial statements of JSC «Thermal Power Plants» were studied in detail. This identified practical problems in the organization's transition process from national to international standards and ways to solve them.

As an empirical research method, the survey method was applied. Questionnaires were conducted with accounting specialists, auditors and financial managers. Using the statistical analysis method, the obtained data were processed and results were interpreted.

Through inductive and deductive thinking methods, transitions from general patterns to particular cases and vice versa, from particular facts to general conclusions, were carried out.

4. Analysis and discussion of results

Financial statement data serves as the main information source for analyzing and auditing the enterprise's financial position. In today's conditions of conducting economic activities, any company's financial statements have never been subject to such detailed and critical analysis. Investors are deeply concerned about various aspects of corporate governance and report preparation, expecting more evidence of data reliability, detailed control and effective activity in the company.

The statement of financial position and its audit is the main document reflecting the value of the enterprise's assets, liabilities and equity on the reporting date. This is the main accounting statement in the IFRS system. In the national accounting standards system, the analog of this statement is the balance sheet. It should be emphasized that the balance sheet is the most important statement required during the audit examination process.

IFRS (IAS) 1 «Presentation of Financial Statements» standard regulates the structure of the statement of financial position. This standard shows the minimum list of items that should be reflected in assets, liabilities and equity. If necessary, the company must disclose them in detail for understanding the financial position. The procedure for grouping assets and liabilities items, the procedure for dividing assets and liabilities into short-term and long-term parts, and the minimum additional information that should be announced in the statement of financial position or in related notes are clearly defined.

The statement of financial position can be prepared in two forms depending on the method of presenting the lines included in it. In the first form, assets and liabilities are presented as short-term (with a period of not more than twelve months from the reporting date or in the normal operating cycle) and long-term. In the second form, they are divided into short-term and long-term assets and liabilities, presented in order of decreasing liquidity. Often the second procedure for preparing the statement of financial position is used by financial institutions.

Current assets are assets that are sold or held for trading purposes within twelve months after the reporting period ends or in the enterprise's normal operating cycle. This also includes cash and cash equivalents. In other cases, assets are classified as long-term. This includes deferred tax assets. If assets meet one of the specific criteria, they are classified as current assets.

A special scheme has been developed to determine current assets criteria.

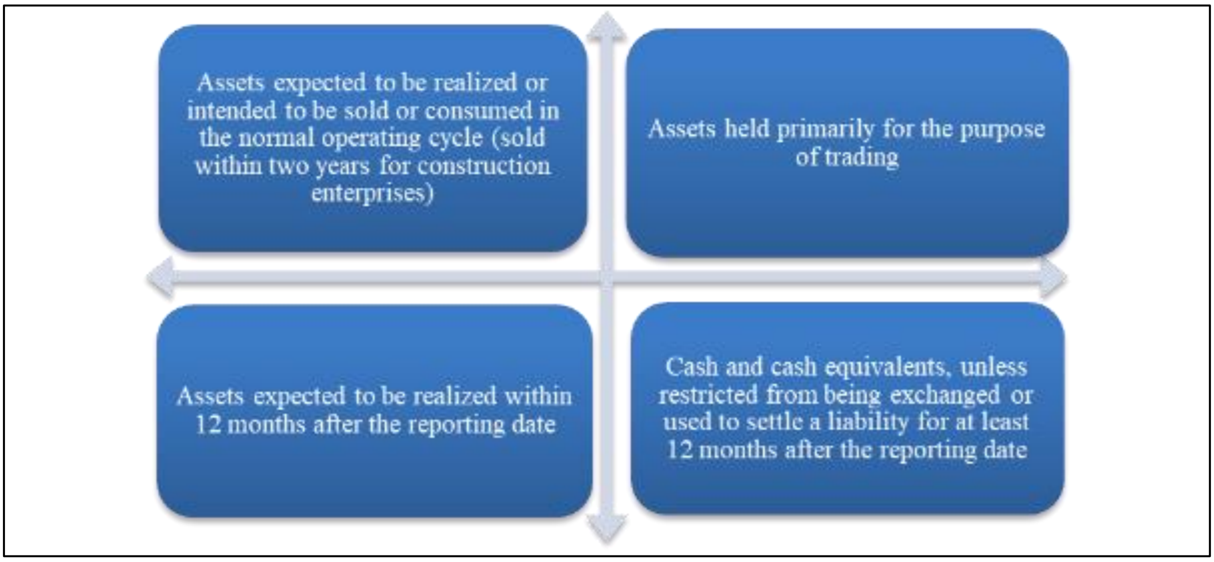

Figure 1 Current Assets Criteria

This scheme shows under what conditions assets are classified as current. Also, a special scheme reflecting short-term liabilities criteria has been developed.

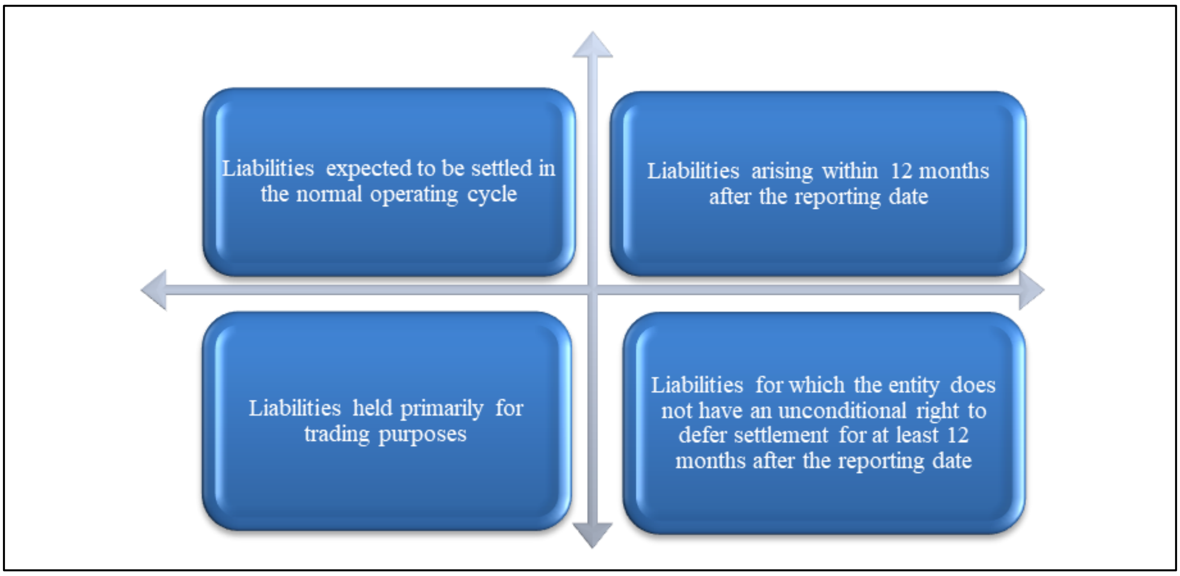

Figure 2 Short-term Liabilities Criteria

A liability is classified as short-term if it meets one of the following criteria. All other liabilities should be classified as long-term. If the enterprise expects to refinance or extend the liability for at least twelve months after the reporting period ends at its discretion under an existing credit line, it classifies this liability as long-term. Deferred tax liabilities are also considered long-term liabilities.

IFRS does not include a mandatory balance format but provides an illustrative example of the statement. Usually two types of statement formats are used in practice. The statement should provide an understanding of the enterprise's financial position and the results of managing resources entrusted to the company. IFRS does not establish a single balance format. IFRS includes a minimum set of elements requiring independent presentation in the statement of financial position, as they differ in nature and functions.

A special scheme has been created to compare formats used in preparing financial statements.

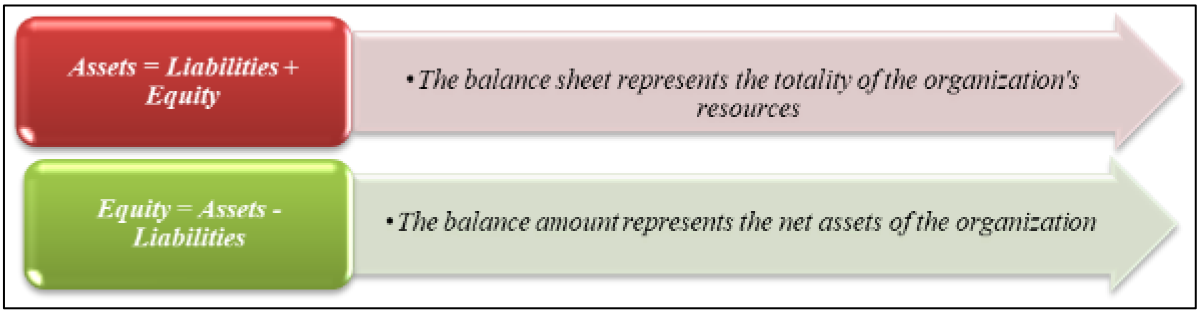

Figure 3 Statement Formats

This scheme shows various methods of preparing the statement of financial position.

These elements include property, plant and equipment, investment property, intangible assets, financial assets, non-current assets held for sale, inventories, tax liabilities, non-controlling interests in equity, parent company's share and others. To form a more complete picture of the organization's position, companies should independently include additional details of statement items. Independent presentation may be based on using different measurement bases for different asset groups.

Today, thanks to the joint efforts of the world's developed countries, a unified accounting system is gradually being created. In modern conditions, transitioning to accounting in accordance with IFRS is an integral part of many enterprises' activities in economic integration processes.

IFRS (IAS) 1 standard regulates the formation of information about financial results in the form of a statement of comprehensive income. At the same time, the statement of comprehensive income should reflect statements containing information about the organization's profit or loss. The statement of comprehensive income contains total financial results and components of other comprehensive income.

During the audit process, no strict requirements are imposed on the statement form according to IFRS. There is no complete list of required information, their location order and names are not regulated, but only a minimum list is defined. This includes revenue, financing expenses, the share of profit or loss of enterprises and joint ventures accounted for using the equity method, tax expenses, profit or loss and others. The specific form of the statement is developed independently by the enterprise.

The auditor can apply two different approaches to grouping statement items in accordance with IFRS (IAS) 1 standard. The nature of expenses method is based on classifying expenses by economic elements and allows disclosing their formation sources. When using the nature of expenses method, determining the financial result of operating activities depends on linking proceeds from sale of products, goods, works and services to changes in the remainder of reporting period expenses.

A special scheme has been developed to compare the two main approaches to grouping expenses.

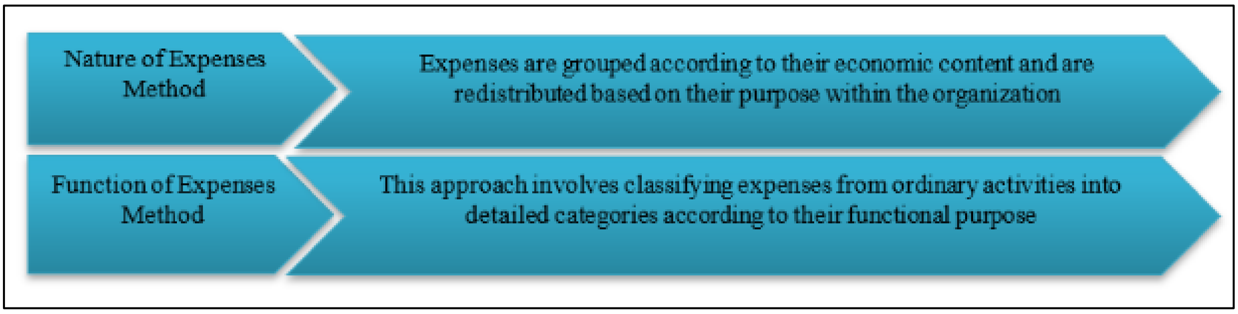

Figure 4 Approaches to Grouping Expenses

This scheme shows the characteristics of the «Nature of Expenses» method and the «Function of Expenses» method.

Calculating financial results using the function of expenses method is based on comparing proceeds from sales with the cost of goods sold. The national statement of financial results, unlike the international version, is presented in an established form and has uniform rules for preparation. The statement format based on IFRS terminology is prepared based on the function of expenses method. It should be noted that enterprises can include explanations in the balance sheet and financial results statement by nature of expenses, which does not contradict IFRS (IAS) 1 standard norms.

The modern form of the financial results statement in the Republic of Uzbekistan ensures calculation of intermediate indicators. This includes gross profit or loss, profit or loss from sales, profit or loss before tax. All income and expenses during the reporting period are divided into those related to carrying out the organization's main activities and income and expenses received through other activities.

The system of minimum indicators announced in the financial results statement includes proceeds from sale of goods, products, works and services. These include VAT tax, excise and other similar taxes and mandatory payments, net profit, cost of sold products, works and services (excluding commercial and administrative expenses), gross income, business expenses, profit or loss from sales, accounts receivable, interest payable.

Also included are other income, other expenses, profit or loss before tax, income tax and other similar mandatory payments, profit or loss from activities, net profit (undistributed profit or uncovered loss). It should be emphasized that despite changes aimed at combining internal and international procedures for disclosing information in the financial results statement, differences still exist between national and international standards.

Based on the above, there are significant differences in the methodology for preparing financial results statement data. For example, differences are observed in terms of disclosure of information about transactions with financial instruments. The statement of comprehensive income includes indicators of income and expenses forming profit or loss for the reporting year, other comprehensive income recognized in the reporting period.

Components of other comprehensive income are as follows. First, gains from revaluation of non-current assets. Second, current gains and losses in pension plans. Third, income and losses arising from disposal. Fourth, income and losses from revaluation of financial assets available for sale. Fifth, the actual part of gains and losses from cash flows.

According to IFRS (IAS) 1 standard, the company has the right to determine the format for presenting the statement of comprehensive income in its accounting policy. It has two forms. The first is a single statement of comprehensive income. The second is a statement of income and a separate statement of other comprehensive income. Also, the company chooses the format of the profit and loss statement itself.

Depending on how income and expenses are shown, there are two types of data development in the income statement. The first is grouping by function within the company. This is analogous to the national income statement and includes revenue, cost of sales, gross income, business expenses, administrative expenses, other income and expenses. The second is grouping income and expenses by characteristics. This includes revenue, other income, changes in finished and work-in-progress inventories, materials used, wages, depreciation, other expenses, profit before tax.

Standards regulating the submission of separate statements include the following. First, IFRS (IAS) 1 standard regulates the form, content and procedure for presenting a complete set of statements. Second, IFRS (IAS) 7 «Cash Flow Statement» standard discloses information about cash and cash equivalents, requirements for classification of cash flows by type of activity. Third, IFRS (IAS) 8 «Accounting Policies, Changes in Estimates and Errors» standard is applied.

International standards for consolidated financial statements include IFRS (IFRS) 3 «Business Combinations» standard. Business combinations are accounted for using the acquisition method in accordance with IFRS (IFRS) 3 standard. According to IFRS (IFRS) 3 standard, identifiable assets, liabilities and contingent liabilities of the acquired enterprise should initially be valued at their fair value on the acquisition date.

Goodwill, after initial recognition, is measured taking into account accumulated losses for impairment. Goodwill is not amortized but must undergo revaluation for impairment at least once a year. Negative goodwill should be immediately recognized as income by the acquirer.

Other standards related to consolidated financial statements include IFRS (IAS) 27 «Consolidated and Separate Financial Statements». IFRS (IAS) 28 standard emphasizes that accounting for investments in associates and combining financial information of associates are carried out using the equity method. IFRS (IAS) 31 «Financial Reporting of Joint Ventures» standard establishes the procedure for reflecting participation in joint ventures.

Preparing statements of profit or loss and other various financial results in accordance with IFRS is intended to reflect the organization's financial results in accordance with IFRS (IAS) 1 standard. It is worth noting that when translated from English (a statement of profit or loss and other comprehensive income), it was translated as «statement of profit or loss and other comprehensive income». However, since the organization may develop not only other comprehensive income but also expenses, the title of this statement was translated as «Profit and Loss Statement and Other Comprehensive Financial Results».

Previously, this statement form was called «Profit and Loss Statement» in IFRS, later it was changed to «Statement of Comprehensive Income» or «Statement of Comprehensive Financial Results». The rules for forming the profit or loss statement and other various financial results are given in IFRS (IAS) 1 standard.

IFRS (IAS) 1 standard defines comprehensive or total financial result (total comprehensive income) and other comprehensive financial result (other comprehensive income). Comprehensive financial income is a change in equity resulting from transactions and other events, excluding changes arising from transactions with founders. It can be concluded that transactions with founders are transactions on depositing and paying dividends.

It is no secret to anyone that the statement of comprehensive income is an updated form of the profit and loss statement. These statement forms should be prepared for any reporting period. Even if one of them is not prepared, financial statements are considered untrue and do not meet international standards requirements. If this situation is detected during an audit examination, in such a case the auditor is obliged to refuse to issue an opinion.

Investors pay more attention to the statement of financial position or simply put the balance sheet and the statement of comprehensive income, the profit and loss statement. Of course, the audit opinion is also very important. The cash flow statement differs fundamentally from other statement forms. It would not be an exaggeration to call it «future-based» because it predicts the organization's potential and prospects. Perhaps this is why a separate standard - IFRS (IAS) 7 «Cash Flow Statement» - was allocated for preparing this statement form.

The cash flow statement is also called «cash flow». Of course, this type of statement complements the statement of financial position and comprehensive income for a certain period. But if the statement of financial position reflects the organization's financial position at a certain moment in time, that is, at the end of the reporting period, and the profit or loss statement reflects the company's activity results for this period, then the cash flow statement determines changes that occurred with one of the components of financial statements from one date of the reporting period to another in cash form.

The information in this statement is useful in that it allows users of financial statements to assess the enterprise's ability to attract cash and cash equivalents and use them. The cash flow statement is the joint existence of two types of statements, namely the statement of financial position and comprehensive income. Therefore, it is prepared after the final statement of financial position, statement of comprehensive income and statement of changes in equity.

The amount of cash and cash equivalents may differ from the statement of financial position and cash flow statement. Therefore, before preparing the statement, an IFRS specialist should make a professional judgment about the amount of cash and cash equivalents, as special emphasis is placed on cash circulation, their flows and of course this statement during the audit process.

The fact that the amount of cash and cash equivalents in the statement of financial position does not equal the amount of cash and cash equivalents in the cash flow statement itself should be indicated in the notes to the financial statements. The cash flow statement is the only statement form prepared without taking into account the accounting method.

According to the requirements of paragraph ten of IFRS (IAS) 7 standard, the cash flow statement should show cash flows for the period classified by operating, investing or financing activities. Using information from accounting records related to numerous transactions involving cash and cash equivalents movements is a difficult task.

There are two methods for preparing the cash flow statement. The first is the direct method. This is a method that discloses the main classes of gross receipts and gross payments, according to which information about the main classes of gross receipts and gross payments can be obtained in two ways. The first is from directly registered registers. The second is using adjustments in appropriate cases from the statement of financial position and comprehensive income.

When preparing the cash flow statement using the direct method, IFRS specialists analyze cash flows in various accounting accounts and classify cash flows according to activity types (operating, financing or investing).

The second is the indirect method. Based on the content of operating activities, it is possible to obtain the cash flow statement using a method opposite to the direct construction algorithm. When using the indirect method, the enterprise's net profit or loss is adjusted according to the results of non-cash transactions, as well as according to changes in operating capital.

In addition to simplicity of calculations, the main advantage of using the indirect method is that it allows showing correspondence between financial results and changes in capital involved in the main activity. In the long term, this method allows identifying the most problematic «accumulation places» of frozen funds and accordingly determining ways out of the situation.

Data availability is an important factor. Separating information necessary for completing the operations section items by the direct method from the organization's total cash flow is basically very difficult, and its formation costs are quite high.

5. Conclusions and recommendations

Research results show that correct assessment and examination of the main forms of financial statements is of great importance in the process of completing audits in accordance with international auditing standards. Financial statements prepared in accordance with IFRS differ from statements based on national standards in a number of aspects. Understanding and correctly assessing these differences requires auditors to have high qualifications and deep knowledge of international standards.

The following practical recommendations are given to auditing organizations. First, when auditing financial statements in accordance with IFRS, it is necessary to study in detail all requirements of international standards. Auditors should know well the latest versions of IFRS (IAS) 1, 7, 8 and other relevant standards. It is necessary to constantly monitor changes made to standards and apply them in practice.

Second, when examining the statement of financial position, special attention should be paid to the correct classification of assets and liabilities. The classification of current and non-current assets, short-term and long-term liabilities must fully comply with IFRS requirements. Auditors should carefully check classification criteria and identify incorrectly classified items.

Third, it is necessary to check that income and expenses are correctly reflected in the financial results statement. It is necessary to determine which method is used - grouping expenses by nature or by functions - and check the consistent application of the chosen method. It is necessary to ensure complete and accurate reflection of income and expenses, as well as to check that they are correctly included in the appropriate period.

Fourth, when examining the cash flow statement, it is necessary to carefully check that cash flows by operating, investing and financing activities are correctly classified. It is necessary to determine which method is used - direct or indirect - and assess whether the chosen method is correctly applied. It is necessary to check the consistency of information in the cash flow statement with the data in the statements of financial position and financial results.

Fifth, when examining consolidated financial statements, it is necessary to check in detail compliance with the requirements of IFRS (IFRS) 3, IFRS (IAS) 27, 28 and 31 standards. It is necessary to check the correct application of the acquisition method in accounting for business combinations, correct determination of goodwill and testing for its impairment. It is necessary to assess the correct application of the equity method in combining financial information of dependent and associated companies.

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