**Revisiting the Application of a Risk-Oriented Audit Approach**

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**Abstract:** This paper discusses the basic understanding of auditing, implemented using approaches and risk management techniques. It emphasizes that such an approach requires the system consideration at all stages: at the stages of planning, collecting audit evidence and completing the project, including the preparation of an audit opinion. Aside from that, the paper presents audit procedures for all phases of the audit which is implemented with account of the risk-oriented approach. The analytical part and the conclusions drawn at end of the work are based on a large number of literature data.

**Introduction**

The introduction of a risk-oriented audit approach is a direct result of widespread risk-oriented methodology in modern analytical studies in virtually all sectors of human everyday practices. Today the risk-oriented approach forms the basis of the requirements of the international standards on auditing. A similar approach is presented in the recommendations of the financial action task force on money laundering (FATF).

The risk-oriented approach allows, on the one hand, to improve the effectiveness of auditors, the level of compliance with obligatory requirements, and on the other, it allows to maximally move away from redundant procedures in audits in the formation of a science-based framework of reasonable sufficiency inherent to each particular audit.

Issues related to risk-oriented auditing have been considered in the works by such scholars as V. Andreev, O.V. Kryshkin.

The sources of information for conducting this study are: ISA 315 "Identifying and assessing the risks of material misstatement through the study of the Organization and its environment" and ACI 330 "Audit procedures in response to assessed risks".

**Analytical part**

For the purposes of this work, the following concepts are made use of:

Risk is the effect of uncertainty on objectives[[1]](#footnote-1)[1].

The system of risk management (ERM) is a set of measures aimed at reducing the risk to an acceptable level by assessing the level of risk of economic entities (objects used by them) and then applying the administrative and legal regimes of the beginning of business, the mandatory requirements and procedures for the exercise of State control (supervision), which are differentiated on the basis of the level of risk of each controlled entity (object)[[2]](#footnote-2)[2].

The risk-oriented approach is a way to implement processes with the use of risk management, which includes the formation of the process objectives, the identification of existing and possible obstacles in achieving these objectives, and the development of measures of reducing the probability of obstacle occurrence and consequences.

The quality of risk management systems differs considerably depending on the type of control. In general, the introduction of a risk-oriented approach can be evaluated according to the quality of two main elements[[3]](#footnote-3)[2]:

* The first element is a system for determining the class of danger.
* The second element is the differentiated approach to the objects under control in dependence to the place in the scale of risk level classification.

The risk-oriented approach to auditing financial statements is enshrined in international auditing standards[[4]](#footnote-4) [3].

It goes without saying that the risk-oriented approach should be implemented at all stages of the audit[[5]](#footnote-5) [4]:

* Planning.
* Collecting audit evidence.
* Completing the project.

During the planning phase, auditors need to implement specific procedures aimed at identifying risk areas associated with likely distortions in the various sections of accounting and reporting. At this stage it is necessary to make a full use of the entire arsenal of risk management techniques, including their identification, classification and development of approaches to respond to risks, i.e. the development of measures facilitating the reduction of the negative impact of the risks identified [[6]](#footnote-6)[5].

In the course of the audit it is necessary to analyze the understanding of the Organization and its environment, including the JMC, by means of:

1. Queries.
2. Analytical procedures.
3. Monitoring and inspection.
4. Assessment of the information received:
* when running the procedure for adopting or continuing the relationships with a customer;
* when performing other tasks for the organization;
* in the previous audit;
* from external sources: industry-specific and trades journals, analytic reports, studies of banks and rating agencies, publications by regulating authorities and financial publications;
* from the answers to the queries addressed to an external lawyer, organization or evaluators whose services were utilized by the organization.

In the framework of implementing the risk-oriented audit approach, the following procedures are to be implemented:

1. Identification and assessment of risks of material misstatement:
* at the level of the financial statements;
* at the level of prerequisite;
1. Formation of an opinion on what risks are significant and an understanding of the relevant means of control of the organization;
2. Identification of risks in respect of which it is impossible/it is impractical to collect sufficient and appropriate audit evidence only on the basis of the substantive procedures, and understanding of relevant means of control of the organization.

To identify whether a particular circumstance is a risk, one should analyze the probability of distortions, including the possibility of multiple distortions, as well as the question of whether the potential distortion is so important that it can lead to a significant distortion.



Figure 1- the matrix of materiality level of audit risk

In order to determine whether the risk is significant, it is essential to:

1. Exclude the influence of the identified means of control pertaining to Fig. 1.
2. Consider the risk against the factors of significance, such as:
* A fraud risk.
* Indicators of to what degree the authorities are involved in accounting issues.
* Significant changes in the economic environment and/or accounting legislation.
* A significant degree of manual intervention in the processes of collecting and processing information on population.
* The accounting staff’s incompetence in certain matters.
* Significant audit corrections in the previous reporting year.
* Frequent and significant changes in trade values.

The task manager must determine which issues should be brought to the attention of the members of the audit team who did not participate in the discussion. A communication plan agreed with the task manager can be of great use. Lack of information distribution is not permissible because then they will not understand:

* The risks of material misstatement in the areas they are responsible for.
* How the results of their audit procedures may affect other aspects of the ongoing audit.
* The need for continuous communication between the members of the audit team.

During the audit while collecting additional audit evidence, assessing the risks of material misstatement at the level of prerequisites can change if the auditor receives new information that contradicts the facts on which their assessment of the risks was initially based.

It is necessary for the auditor to include in the audit documentation:

* Discussions between the members of the audit team and important decisions made.
* The key elements of understanding each aspect of the organization and its environment and each element of its JMC. The sources of information from which this understanding has been obtained; as well as completed risk assessment procedures.
* Identified and assessed risks of material misstatement at the level of financial reporting and at the level of the premises.
* Identified significant risks/risks in respect of which it is impossible/it is impractical to collect sufficient appropriate audit evidence only on the basis of the substantive procedures, and controls related to such risks.

Risk assessment is an ongoing dynamic process of collecting, updating and analyzing information throughout the audit "[[7]](#footnote-7)[6].

The results of the risk assessment are the basis of the formation of the strategy/audit plans, as they allow to judge:

* For which articles there are effective controls.
* Which articles are prone to build analytical expectations.
* How it is possible to streamline the approach to the selection of items for detailed testing.
* How to interpret the results of any audit procedure.

It is necessary for the auditor to develop and execute:

1. In response to assessed risks at the level of financial reporting – audit procedures of general nature.
2. In response to assessed risks at the level of prerequisite – audit procedures of a specific nature, timing and amount.

Independent or checklist (combined) can affect the approach to auditing premises.

In the course of auditing practices, the following instances of financial reporting risk were found:

* The directorship’s ability to avoid controls.
* The problem of continuity of operations.
* Change in the key personnel, who influence the quality of financial reporting.
* A detailed understanding of the audit methodology by the directorship.
* A more detailed, thorough and general survey of the working documentation.
* Further review (by a concurring review partner).
* Involvement of experts and/or more experienced auditors.
* Use of unpredictability in audit procedures.
* Changes in the nature, timing or extent of audit procedures.

Directly within the audit, it is necessary for the auditor to maximally fully implement all the planned risk management procedures, taking into account the facts and circumstances identified. In doing so, the auditor is to include (if necessary) clarifications and additions in the original risk management plan[[8]](#footnote-8)[7].

At the final stage, the auditor should pay maximal attention to the risks associated with the formation of reporting for the customer. This step is considered the quintessence of the risk management process. As at the final step it is necessary to analyze the full array of information assembled during the planning phase of the project and its implementation. If the auditor plans to use the evidence of operational efficiency of the control means which were tested during the previous audit, he/she should include their conclusions regarding their reliance on these control means in the audit documentation. The audit documentation should contain evidence that the financial statements have been verified via the subjacent accounting data[[9]](#footnote-9)[8].

**Conclusion**

The characteristic feature of our time which defines the border of the New era (seventeenth century) is mastering the strategy of behavior in the presence of risk. This strategy is based on the understanding of the fact that future is not just a "whim of the gods", but the result of deliberate human activity. In our opinion, the formation of the ideology of risk-oriented auditing is a kind of transition to a new era of audit[[10]](#footnote-10) [9].

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