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AICPA	American Institute Certified Public Accountants
COSO	Committee of Sponsoring Organization
DCAA	Defense Contract Audit Agency
FASB	Financial Accounting Standards Board
GAAP	Generally Accepted Accounting Principles
GAAS	Generally Accepted Auditing Standards
GAGAS	Generally Accepted Government Auditing Standards
GAO	Governmental Auditing Organization
IRS	Internal Revenue Services ()
IFAC	International Federation of Accountants
IIA	International Internal Auditing
PATACS	Palestinian Authority Tax Administration Computer Services
SEC	Security Exchange Commission
SASS	Statement on Auditing Standards
SRTPS	Statement on Responsibilities in Tax Practice

SSARS	Statements on Standard for Accounting and Revenue Services
SSAES	Statements on Standards for Attestation Engagements
VAT	Value Added Tax

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"Auditing is a systematic process of objectively obtained and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria and communicating the results to interested users".

: (2) Alvin A. Arens

"Auditing is the accumulation and evaluation of evidence about information to determine and report on the degree of correspondence

¹⁾ American Accounting Association, **Committee on Basic Concepts**, Sarasota, FL, AAA, 1973, in: Messier, William F. Jr .(2000), **Auditing and Assurance Services** , 2nd Ed. Boston ,P.11

- William C., Boynton and others, **Modern Auditing**, 5th. Ed. 1996. Jhon Willy & Sons, Inc., P. 4

²⁾Arens Alvin A and others, **Auditing and Assurance Services**, Person Education, Inc., 9 Ed. 2003 .P.9

between the information and established criteria, and should be done by a competent, independent person."

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Systematic Process .1

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Spirit of auditing means: It is unnecessary to follow the standards blindly, the auditor is justified in following an alternative course of action so, the burden of justifying departures from the standards fall on the auditor.

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Assurance Services :

Assurance Services		
Attestation Services		Certain Management Consulting
Audits	Review	
Other Attestation Services (e.g.,) Web Trust,Sys Trust)		

None Assurance services :

Other Management Consulting
Certain Management Consulting
Accounting and Bookkeeping
Tax Services

Other Assurance Service⁽²⁾ :

Other Assurance Services Example	
Other assurance services	Service activities
Controls over and risk related to investments, including policies related to derivatives	Asses the process in a company's investment practices to identify risks and to determine the effectiveness of those process
Mystery shopping	Perform anonymous shooing to assess sales personnel dealings with customers and procedures they follow
Asses risk of accumulation, distribution, and storage of digital information	Assess security risks and related controls over electronics data, including the adequacy of backup and off-site storage
Fraud and illegal acts risk	Develop fraud risk profiles and

⁽¹⁾ Arens.Alvin A and others, **Auditing and Assurance Services**, Person Education, Inc., 9 Ed. 2003 .P.9

(2) Ibid, Arens Alvin A and others, P.9

assessment	assess the adequacy of company systems and policies in preventing and detecting fraud and illegal acts
Compliance with trading policies and procedures	Examine transactions between trading partners to ensure that transactions comply with agreements; identify risks in the agreement

: ⁽¹⁾Boynton

Financial Statement Audit	- 1
Compliance Audit	-2
Operational, Performance or Management Audit	-3
Forensic Audit or Investigation	-4

: Boynton

Attestation Services	- 1
Financial Audit	-2
Examination	-3
Review	-5
Agreed –Upon Procedures	-6
Non-attestation Services	-7
Accounting Services	-8
Taxation	-9
Consulting Services	-10

: Boynton Messier

⁽¹⁾ Boynton, Williams and others, **Modern Auditing**. 6th.Ed. 1996. Jhon Willy& Sons, Inc.Canada, P. 4

Independent Auditors	-1
Internal Auditors	-2
Government Auditors	-3

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Financial Statement Audit	-1
Compliance Audit	-2
Operational Audit ()	-3
Forensic Audit or Investigation ⁽²⁾	-4

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⁽¹⁾ Messier, William, Ibid, P, 13.

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⁽²⁾ Forensic Audits means: A forensic audits purpose is the detection or deterrence of a wide variety of fraudulent activities and include: * Business or employee fraud; * Criminal investigation; * Shareholder and partnership disputes; * Business economic losses; * Matrimonial disputes

pre-audits : -

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Compliance Audits : -2

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Operational Audit

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"An operational audit involves a systematic review of organization activities or a part of them, in relation to the efficient and effective use of resources".

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Performance Audit or Management Audit

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Operational or management or performance auditing	Financial auditig
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Efficiency and effectiveness	
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Inclusion of Nonfinancial Areas

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Efficiency and Effectiveness	Substantive audit testing
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Examples of the three Types of Audits				
Type of audit	Example	Information	Established Criteria	Available Evidence
Operational audit	Evaluate whether the computerized payroll processing for subsidiary records is operating effectively	Number of payroll records processed in a month, cost of the department, and number of errors	Company standards for efficiency and effectiveness in payroll department	Error reports, payroll records and payroll processing costs
Operational audit				
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Compliance audit	Determine whether bank requirements for loan continuation have been met	Company records	Loan agreement provisions	Financial statements and calculations by the auditor
Financial statement audit	Annual audit of Boeing's financial statements	Boeing's financial statements	Generally accepted accounting principles	Documents, records, and outside sources of evidence

Boeing :

(1) Ibid , Arens, Alvin A. and others .P.15

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Compliance Audit

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Compliance audit

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The internal Revenue Services (IRS) defined a tax “an enforced contribution, exacted pursuant to legislative authority in the exercise of the taxing power, and imposed and collecting for the purposes of raising revenue to be based for public or governmental purposes. Taxes are not payments for some special privilege granted or service rendered and are, therefore, distinguishable from various other charges imposed for particular purposes under particular powers or functions of government .”⁽¹⁾

(IRS)

⁽¹⁾ Murphy, Kevin E. **Concept in Federal Taxation**. West Publishing Company, U.S.A, Ed.8, 1994. P.4

Characteristics of tax

- 1- The payment to the government authority is required by law.
- 2- The payment is required pursuant to the legislative power to tax.
- 3- The purpose of requiring the payment is to provide revenue to be used for public or governmental purposes.
- 4- Special benefits, services, or privileges are not received as a result of making the payment. The payment is not a fine or penalty that is imposed under other powers of government ⁽¹⁾.

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⁽¹⁾ Ibid ,Murphy, Kevin E.P.5

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⁽¹⁾ Shoup, C. and Others, (1985). **Report on Japanese Taxation by the Shoup Mission.** General head quarters, Kassoumi Publishing Co. Tokyo P 1

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The Additive side [wages + profits]

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The Subtractive – Direct method [Out Puts – Inputs] * Rate

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(1) Ibid, Shoup , C. and others P 14

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The Subtractive – Indirect method

Rate x Outputs - Rate x Inputs

The Subtractive – Indirect method

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Transaction

Tax Liability

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The Cascade Tax"

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The Original EC The Invoice or Credit method.

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⁽¹⁾ Ibid, Tiat, P 5

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(General Cooncept) ⁽¹⁾

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(General Concept)

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1- General Concept

"General concepts provide guidance on the overall operation and implementation of the income tax system. As such, these concepts apply to almost every aspect of the system, be it an accounting issue, an income issue, or a deduction issue".

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2- Ability-To-Pay Concept

⁽¹⁾ Ibid, Murphy, Keven E. ,P.4

3- Administrative Convenience Concept

4- Arm's –Length Transaction Concept

"An arm's- length transaction is one in which all parties to the transaction have bargained in good faith and for their individual benefit, not for the benefit of the transaction group ⁽¹⁾".

5- Pay- As- You- Go Concept

⁽¹⁾ Ibid, Murphy, Keven. E.P.6

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- 1- Entity concept
- 2- Annual Accounting Period Concept
- 3- All- Inclusive Income Concept
- 4- Legislative Grace Concept
- 5- Capital Recovery Concept
- 6- Realization Concept
- 7- Constructive Receipt Doctrone
- 8- Wherewithal- to- pay Concept

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(1) Ibid, Murphy, Keven. E.P.7

Postulates of Taxation :

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⁽¹⁾ Eric, Kholer, **A dictionary for accounting**, 4th Ed. Prentice Hall, Inc., 1970,P.100

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Systematic Audit Approach

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"Ethics can be defined broadly as a set of moral ptinciples or values."⁽¹⁾

Illustrative Prescribed Ethical Principles

The following are the six core ethical values that the Josephson Institute associates with ethical behavior.

- 1- Trustworthiness:() includes honesty, integrity, reliability,and loyalty.
- 2- Respect: includes notions such as civility,courtesy, dignity, tolerance,and acceptance.
- 3- Responsibility: means being accountable for one's and exercising restraint.

⁽¹⁾ Ibid, Arens, Alvin A , P.74

- 4- Fairness: and justice includes issues of equality, impartiality, proportionality, openness, and due process. Fair treatment means that similar situations are handled consistently.
- 5- Caring: means being genuinely concerned for the welfare of others and includes acting altruistically and showing benevolence
- 6- Citizenship: includes obeying laws and performing one's fair share to make society work, including such activities as voting, serving on juries, and conserving resources " .

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Independency, Integrity & Objectivity :-2

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Insiders

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⁽¹⁾ Hendrickson, E.S. **Accounting Theory**, 3 rd Ed., Homewood III .R.D Irwin,U.S.A,1977, P.1

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⁽¹⁾ Ibid, Arens, Alvin A, P.97

Summary of rules of conduct .1-2

Topic	All Members	Member in Public Practice	Summary of Rules
Independence		X	A member in public practice shall be independent in the performance of professional services as required by standards promulgated by bodies designated by council
Integrity and objectivity	×		In performing any professional services, a member shall maintain objectivity and integrity, shall be free of conflicts of interest, and shall not knowingly misrepresent facts or subordinate his judgment to others
General standards	×		For all services, a member shall comply with the following professional standards and interpretations thereof by bodies designated by council: (1) undertake only those professional services that the member can reasonably expect to complete with professional competence,(2) exercise due professional care.(3)adequately plan and supervise all engagements, and(4) obtai sufficient relevant data to afford a reasonable basis for all conclusions or recommendations.
Compliance with standards	×		A member who performs auditing, review, compilation, management consulting, tax, or other professional services shall comply with standards promulgated by bodies designated by council
Accounting principles-	×		A member shall follow the professional audit reporting standards promulgated by bodies designated by council in issuing reports about entities, compliance with generally accepted accounting principles
Confidential client information		x	A member in public practice shall not disclose any confidential client

			information without the specific consent of the client.
Contingent fees		x	A member in public practice shall not perform for a contingent fee any professional service if the member also performs for the client an audit, review, or certain compilations of financial statements, or an examination of prospective financial statements. A member in public practice should also not prepare an original or amended tax return or claim for a tax refund for a contingent fee for any client
Act discreditable	x		A member shall not commit an act discreditable to the profession
Advertising and others form of solicitation		X	A member in public practice shall not seek to obtain clients by advertising or other forms of solicitation in a manner that is false, misleading, or deceptive. Solicitation by the use of coercion, overreaching, or harassing conduct is prohibited
Commission and referral fees		X	A member in public practice shall not receive or pay a commission or referral fee for any client if the member also performs for the client an audit, review, or certain compilations of financial statements, or an examination of prospective financial statements. For nonprohibited commissions or referral fees, a member must disclose the existence of such fees to the client
Form of organization and name		x	A member may practice public accounting only in a form of organization permitted by state law or regulation whose characteristics conform to resolutions of council and shall not practice public accounting under a firm name that is misleading

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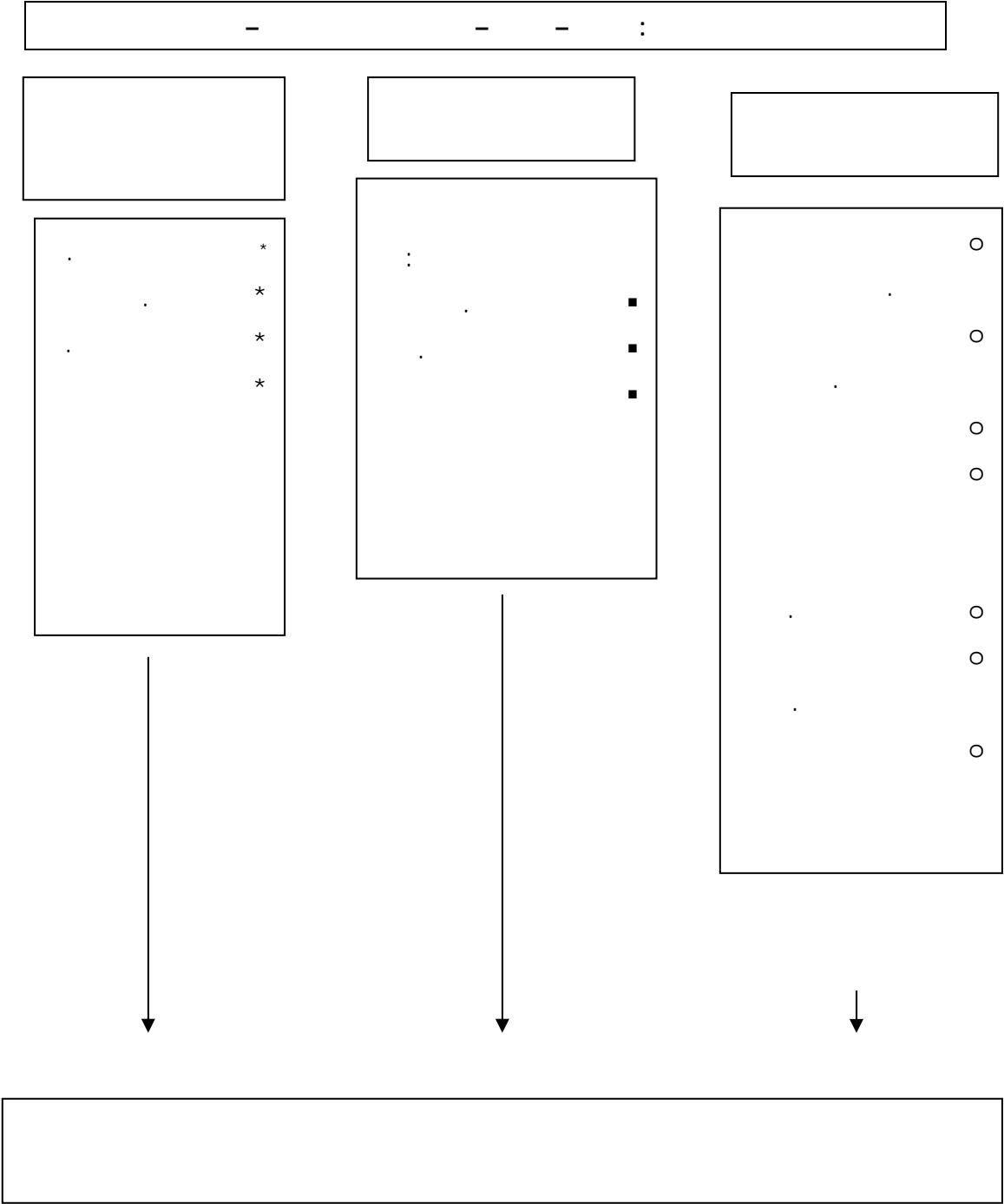
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Services

The Right Tax at the Right Time from the Right person.

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Main reasons why a conceptual framework of accounting is important.

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⁽¹⁾ Kieso, Donald E , **Intermediate Accounting**, John Wiley & sons, Inc. U.S.A, 10.Ed. P.34

- 1- Prescribes the boundaries of accounting and financial reporting
- provides definitions of basic objectives
- Provides key terms of the financial statements
- Provides fundamental concepts

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- 2- Assists the standards- setting body in developing new standards and revising previously issued accounting and reporting standards.

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- 3- Helps users of financial statements to understand the purpose and contents of information provided.

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- 4- Assists accountants in selecting from among alternatives the most appropriate method that most accurately reflect the results of operations and the financial position of the entity.

Major components of conceptual frame work of accounting

- * objectives
- * concepts
- * guidelines
- * traditional assumptions

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Compliance Audit

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Systematic Process

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"An audit process is a well-defined methodology for organizing an audit to ensure that the evidence gathered is both sufficient and competent and that all appropriate audit objectives are both specified and met."

⁽¹⁾ Ibid, Arens, Alvin A, P.357

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Arens⁽¹⁾

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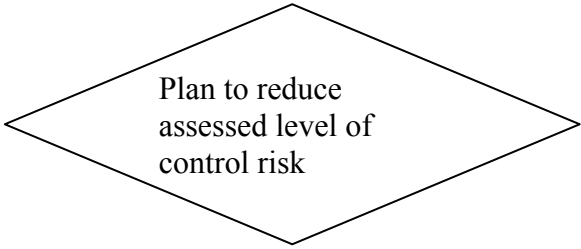
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⁽¹⁾ Ibid, Arens, Alvin A, P.357

Phase 1	Plan and design an audit approach
	Accept client and perform initial planning
	Understand the client's business and industry
	Assess client business risk
	Perform preliminary analytical procedures
	Set materiality and assess acceptable audit risk and inherent risk
	Understand internal control and assess control risk
	Develop overall audit plan and audit program
Phase 2	Perform tests of controls and substantive tests of transactions
	 <p>Plan to reduce assessed level of control risk</p>
	Perform tests of control
	Perform substantive tests of transactions
	Assess likelihood of misstatements in financial statements
Phase 3	Perform analytical procedures and tests of details of balances
	Low Medium High or unknown
	Perform analytical procedures
	Perform tests of key terms
	Perform additional tests of details of balance
Phase 4	Complete the audit and issue an audit report
	Review for contingent liabilities
	Review for subsequent events
	Accumulate final evidence
	Evaluate results
	Issue audit report
	Communicate with audit committee and management

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Premature Conclusion

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Cause and Effect

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(1) Forensic Audit
Compliance Audit

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Statement on Responsibility in Tax Practice
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⁽¹⁾ Avens, Alvin A and others, Ibid, P.13
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Due Care

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Prudent Person Concept or Standards of due care

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He is liable to his employer for negligence, bad faith, or dishonesty, but not for losses consequent upon pure errors of judgment.

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SAS 94

: ⁽²⁾ (COSO)

“ Internal control is a process, effected by an entity’s board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

⁽¹⁾ Ibid. Arens, Alvin A. P. 282

⁽²⁾ Committee of Sponsoring Organizations of the Treadway Commission (COSO)

- Reliability of financial reporting
- Compliance with applicable laws and regulations
- Effectiveness and efficiency of operation "

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Arens

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Components of Internal control		
Internal control		
Components	Description of components	Further subdivision(if applicable)
Control environment	Actions, policies, and procedures that reflect the overall attitude of top management, directors, and owners of an entity about internal control and its importance	Subcomponents of the control environment: <ul style="list-style-type: none"> • Integrity and ethical values • Commitment to competence • Board of directors or audit committee participation • Management

⁽¹⁾ Ibid. Arens, Alvin A. P. 282

		<p>philosophy and operating style</p> <ul style="list-style-type: none"> • Organizational structure • Assignment of authority and responsibility • Human resource policies and practices
Risk assessment	Management's identification and analysis of risks relevant to the preparation of financial statement in accordance with GAAP	<p>Risk assessment processes :</p> <ul style="list-style-type: none"> *Identify factors affecting risks *Assess significance of risks and likelihood of occurrence *Determine actions necessary to manage risk <p>Management assertions that must be satisfied:</p> <ul style="list-style-type: none"> *Existence or occurrence *Completeness *Valuation or allocation *Rights and obligations *Presentation and disclosure
Control activities	Policies and procedures that management has established to meet its objectives for financial reporting	<p>Types of specific control activities:</p> <ul style="list-style-type: none"> • adequate separation of duties • Proper authorization of transactions and activities • Adequate document and records • Physical control over assets and records • Independent checks

		on performance
Information and communication	Methods used to initiate, record, process, and report an entity's transaction and to maintain accountability for related assets	Transaction-related audit objectives that must be satisfied: *Existence *Completeness *Accuracy *Classification *Timing *Posting and summarization
Monitoring	Management's on going and periodic assessment of the quality of internal control performance to determine whether controls are operating as intended and modified when needed	Not applicable

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Obtain understanding of internal control. Design and operation	Assess control risk	Test controls	Decide planned detection risk and substantive tests
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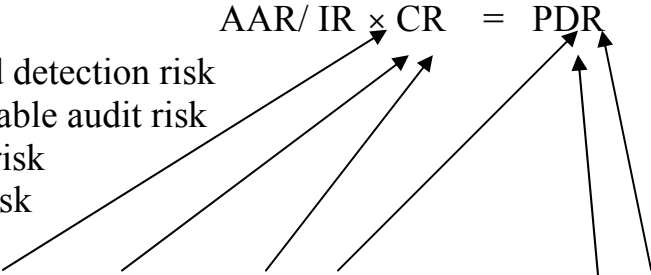
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Controls over classes of transactions

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Procedures to obtain an understanding of internal control;						
	Types of audit Tests and the Audit Risk Model					
Audit Risk Model	$AAR/IR \times CR = PDR =$ <p> PDR= Planned detection risk AAR= Acceptable audit risk IR= inherent risk CR= control risk </p> 					
Type of audit Tests	1- Procedures to obtain an understand of internal control	2- Tests of control	3- Substantive tests of transactions	4- Analytical procedures	5- Test of details balances	6- Sufficient competent evidence per GAAS
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⁽¹⁾ Ibid, Arens, Alvin A. P.338

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GAAP

GAAS

⁽¹⁾ F. Jr Messier

GAAS

Audit Activities

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⁽¹⁾Ibid, Messier, F. Jr P.752-755

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Planning the Tax Audit

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Gathering Evidence of Performance

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Analysis and Investigation of Deviation	-3
Determining Corrective Action	-4
Reporting the Results of an Audit Tax	-5

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Types of Tax Audits : :-3

Credit Returns : :3-1

A frequent source of fraud and error

Verification

First Audits : :3-2

Large vender audits :3-3

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Revenue recovery audit	:3-4
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Compliance audits	:3-5
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Finals / Others	:3-6
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Immediate Audit

Deterrence Audits	:3-7
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(Tax Fraud) :4-1

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(Underreporting) :4-2

(Avoidance) :4-3

Loopholes in Tax Laws

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⁽¹⁾ Ibid, Alan A Tait, P.67 .

⁽²⁾

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preparation	-1
Planning	-2
Verification	-3
Evaluation	-4
Reporting	-5
Record	-6
Establish	-7
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"The CPA may serve as an expert witness in behalf of the Taxpayer. He may also develop an opinion as to whether transactions have been interpreted and recorded in conformity with GAAP" ⁽¹⁾.

"In attempting to prove tax evasion , the government may rely on evidence that the Taxpayer net worth has increased during the year by an amount greater than the reported income ⁽²⁾ ."

Panning :7-3

Priorities

.Efficient use of resources

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Pre- visit :

⁽¹⁾ Walter B. Meigs and others, **Principles of Auditing**, 5th Ed 1973 Homewood, Illinois, 5th. Ed. P. No.105.

⁽²⁾ Ibid, Walter B.Meigs and others.P.105

.CPA

During the visit :

Post visit :

Assurance Credibility

Verification :7-4

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Compliance Testing *

Substantive Testing *

Evaluation :7-5

Walkthrough

"At this stage you will have gathered considerable information in relation to the accounting system you are auditing and the need now is to evaluate the findings to determine what they tell you about the inherent strengths and weaknesses of the system" ⁽¹⁾.

Recording : :7-6

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The Right Tax at the Right time from the Right Person.

Establishment : : 7-7

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⁽¹⁾ Ernst & Young, **Enhanced Accountancy & Audit training**. 1999. p.5

To carry out tax assurance duties effectively and maximise traders compliance.

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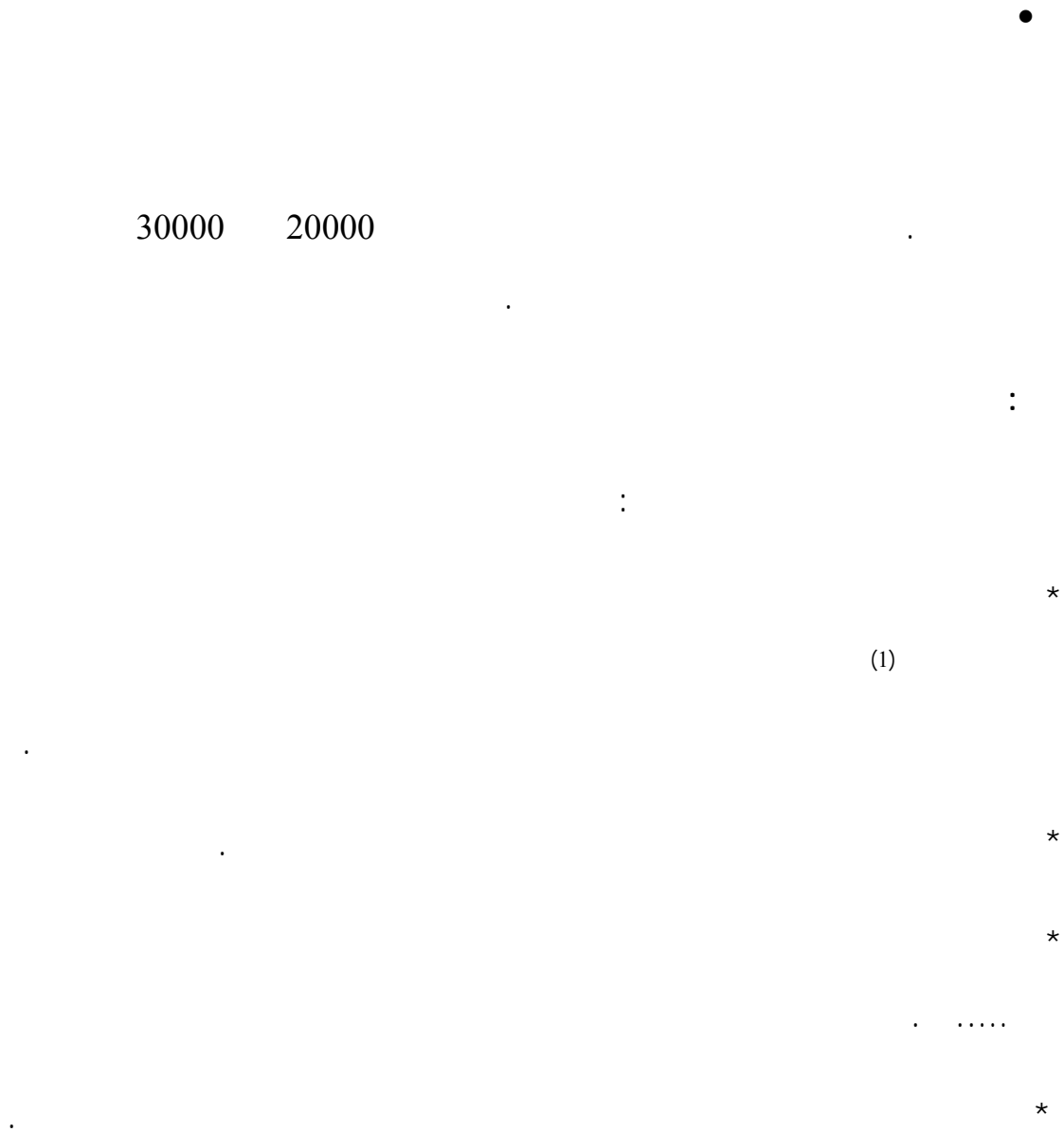
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GAAS

Globalization of business and capital markets

International standards on Auditing (ISAs)

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(IFAC)

International Federation of Accountants (IFAC)

(GAAS)

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Summary of Generally Accepted Auditing Standards		
Generally Accepted Auditing Standards		
General qualifications and conduct (General Standards)	Field work performance of the audit (Standards of field works)	Reporting results (Standards of Reporting)
1- Adequate training and proficiency	1- Proper planning and supervision	1- Whether statements were prepared in accordance with GAAP
2- Independence in mental attitude	2- Sufficient understanding of internal control	2- Circumstances when GAAP not consistently followed
3- Due professional care	3- Sufficient competent evidence	3- Adequacy of informative disclosures
		4- Expression of opinion of financial statements

SAS1 (AU 110)

GAAS

SAS 1 (AU 110) states

The objective of the ordinary audit of financial statements by the independent auditor is the expression of an opinion on the fairness with which they present fairly in all material respects, financial positions, results

of operations, and its cash flow in conformity with generally accepted accounting principles.

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- Standard unqualified
 - 1-All statements- balance sheet, income statement of retained earnings,and statement of cash flows-are included in the financial statements
 - 2- Sufficient evidence has been accumulated
 - 3- F.S are presented according to GAAS
 - 4- Adequate disclosure have been included in the footnotes
- Unqualified with explanayory paragraph of modified wording

A complete audit took place with satisfactory results and financial statements that are fairly presented,but the auditor believes that it is important or is required to provide additional information
- Qualified

The auditor concludes that the overall financial statements are fairly presented, but the scope of the audit has been materially restricted or generally accepted accounting principles were not followed in preparing the financial statements.
- Adverse or disclaimer

The auditor concludes that the financial statements are not fairly presented (adverse), he is unable to form an opinion as to whether the financial statements are fairly presented (disclaimer), he is not independent (disclaimer)

⁽¹⁾ Ibid, Arens, Alvins A. P.49

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SAS 1 (AU110)

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The auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements, whether caused by error or fraud. Because of the nature of audit evidence and the characteristics of fraud, the auditor is able to obtain reasonable, but not absolute, assurance that material misstatements are detected. The auditor has no responsibility to plan and perform the audit to obtain reasonable assurance that misstatements, whether caused by error or fraud, that are not material to the financial statements are detected.

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⁽¹⁾ Ibid, Arens ,Alvin A. P.111

Legal term	Description
Terms Related to Negligence and Fraud	
Ordinary negligence	Absence of reasonable care that can be expected of person in a set of circumstances for auditors, it is in terms of what other competent auditors would have done in the same situation
Gross negligence /	Lack of even slight care, tantamount to reckless behavior, that can be expected of a person.
Constructive fraud	Existence of extreme or unusual negligence even though there was no intent to deceive or do harm. Constructive fraud is also termed recklessness. Recklessness in the case of an audit would be present if the auditor knew an adequate audit was not done but still issued an opinion, even though there was no intention of deceiving statement users
Fraud	Occurs when a misstatement is made and there is both the knowledge of its falsity and the intent to deceive : -1 -2 -3 -4
Terms Related to Contract Law	
Breach of contract	Failure of one or both parties in a contract to fulfill the requirements of the contract. An example is the failure of a CPA firm to deliver a tax return on the agreed-upon date. Parties have a relationship that is established by a contract are said to have privity of contract

Third- party beneficiary	A third party who does not have privity of contract but is known to the contracting parties and is intended to have certain rights and benefits under the contract. A common example is a bank that has a large loan outstanding at the balance sheet date and requires an audit as a part of its loan agreement.
Others Terms	
Common law	Laws that have been developed through court decisions rather than through government statutes
Statutory law	Laws that have been passed other governmental units
Joint and several liability	The assessment against a defendant of the full loss suffered by a plaintiff, regardless of the extent to which other parties shared in the wrongdoing. For example, if management intentionally misstates financial statements, an auditor can be assessed the entire loss to shareholders if the company is bankrupt and management is unable to pay
Separate and proportionate liability	The assessment against a defendant of that portion of the damage caused by the defendant's negligence. For example, if the courts determine that an auditor's negligence in conducting an audit was the cause of 30% of a loss to a defendant, only 30% of the aggregate damage would be assessed to the CPA firm

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Systematic Tax Audit Approach

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Systematic Audit Approach

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The Right Tax at the Right time.

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Practical

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Consistent and functionally useful

The Right Tax at the Right Time from the Right Person

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⁽¹⁾International Monetary Fund (F.A.D), **Recommendation for further improvement of fiscal administration**, Ministry of Finance, Ramalla, Palestine. 1999. P. 40-41.

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⁽¹⁾ Ibid, Alan Tait p.67.

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Milka Casanegra

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Tax administration may be thought of as a series of links making up a chain. The strength of the weakest link determines the strength of the chain as a whole, when tax administration is weak, tax administration will also be weak.⁽¹⁾

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Engagement planning involves all the issues the auditor should consider in developing an overall strategy for conducting the audit ⁽²⁾."

⁽¹⁾ Ibid, Alan Tait, P. 67.

⁽²⁾ Ibid ,Ernest .Young, P.2

:Ernest Young

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Ernest Young

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Planning an Audit and Designing an Audit Approach
Accept client and perform initial audit planning
Understand the client's business and industry
Assess client business risk
Perform preliminary analytical procedures
Set materiality and assess acceptable audit risk and inherent risk
Understand internal control and assess control risk
Develop overall audit plan and audit program

.Systematic audit approach

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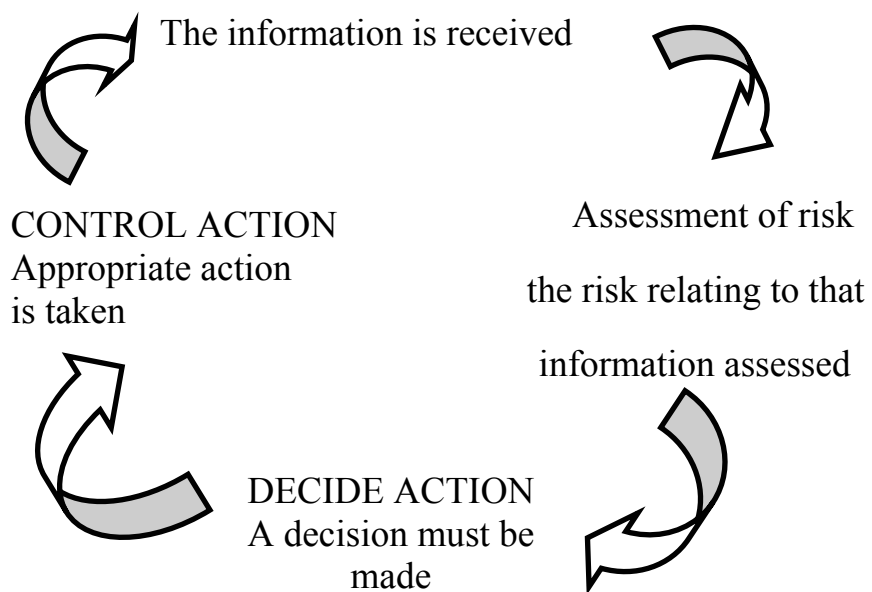
Audit risk

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INFORMATION



⁽¹⁾ Ibid, Ernst & Young P.6.

VAT Assurance

Specific credibility checks

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The Right Tax at the Right time.

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Audit trail

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Audit trail is: a means for verifying the completeness of accounts by the tracing forward or backward, through the system of data. It is the route by which a transaction has been processed through the system, and can be traced using documents such as reports, orders, invoices⁽¹⁾.

: Audit trail

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⁽¹⁾ Ibid, Ernest & Young, unit 4.

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Key Control-:

Key Controls ()

Key controls: is a manual or systems control specifically in place to ensure the correctness of the accounting procedures.

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Analytical audit

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⁽¹⁾ Ibid, Kieso & others . P. 215
-Ibid, Arens, Alvin A .P. 208

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⁽¹⁾Ibid, Ernst &Young, Unit 2, P.4
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	Audit failure		-2
Erroneous audit opinion			
.GAAS			
	Breach of duty of care		
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	Audit Risk		-3
	Due care		
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:	Walter \ Booynton	Audit Risk :	

Audit Risk: “is the risk that the auditor may unknowingly fail to appropriately modify the opinion on Financial Statement that are materially misstated ⁽¹⁾”.

Reasonable Assurance

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Qualified

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PDR

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AAR / IR X CR

Planned detection risk

Acceptable audit risk

Inherent risk

Control risk

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IR

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CR

100%

AAR

5%

PDR

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GAAS

Types of risk

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Planned detection risk

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Inherent risk

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Control risk

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⁽¹⁾ Walter B. Kell and others, **Modern Auditing**, 6th. Ed. U.S.A, 1996 .P231

⁽¹⁾ Ibid , Arens ,Alvin A. P.241

Acceptable audit risk :

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Tolerable amount

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.Substantive evidence

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Inherent Risk :

Segments errors or fraud

Effectiveness of internal control

Susceptibility of the financial statement

.High inherent risk

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Warranty		-3
	.obligation	
Technological developments		-4

- *Nature of the client's business
- *Results of previous audits
- *Initial versus repeat engagement
- *Related parties
- *Nonroutine transactions
- *Judgment required to correctly record account balances and transactions
- *Makeup of the population
- *None Compliance with Tax Law

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The auditor cannot guarantee the complete absence of material misstatements.

Audit Assurance

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The auditor cannot guarantee the complete absence of material misstatements .

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Methods Practitioners Use to Assess Acceptable Audit Risk	
Factors	Methods Used to Assess Acceptable Audit Risk
External users reliance on financial statements	<ul style="list-style-type: none"> *Examine the financial statements, including footnotes *Read minutes of board of directors meeting to determine future plans. *Discuss financing plans with management
Likelihood of financial difficulties	<ul style="list-style-type: none"> • Analyze the financial statement for financial difficulties using ratios and other analytical procedures. • Examine historical and projected cash flow statements for the nature of cash inflows and outflows
Management integrity	<ul style="list-style-type: none"> • Accept client and perform initial planning • Understand the client's business and industry • Assess client business risk • Perform preliminary analytical procedures

⁽¹⁾ Ibid , Arens, Alvin A. P.245

Conducting Tax Assurance Work

Approach Cycle

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Sales and collection cycle	
Auditors assesment of material misstatement before considering internal control	Expect some misstatement Medium
Auditor's assessment of effectiveness of internal controls to prevent or detect material misstatements (control risk)	Medium effectiveness
Auditor's willingness to permit material misstatements to exist after completing the audit (Acceptable audit risk)	Low Willingness (Low)
Extent of evidence the auditor plans to accumulate (Planned detection risk)	Medium level (Medium)

Materiality :

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"The magnitude of an omission or misstatement of accounting information that, in the light of surrounding circumstances, makes it probable that the judgment of the reasonable person relying on the information would have been changed or influenced by the omission or misstatement".

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Materiality is a relative than an absolute concept

⁽¹⁾ Ibid ,Arens, Alvin A. P. 232

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Bases are needed for evaluating materiality

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Qualitative factors also affect materiality

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Steps in applying materiality	
Planning extent of tests (step 1+ step 2)	
Set preliminary judgment	Step 1
Allocate preliminary judgment about materiality to segments	Step 2
Evaluating results (step 3+4+5)	
Estimate total misstatement in segments	Step 3
Estimate the combined misstatement	Step 4
Compare combined estimate with preliminary or revised judgment about materiality	Step 5

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Type of Opinion أنواع التقارير	Significance in terms of reasonable users' decisions الاهمية من قبل المستخدمين	Materiality level مستوى الاهمية
Unqualified تقرير نظيف	Users, decisions are unlikely to be affected	Immaterial غير مهم
Qualified تقرير غير نظيف	Users, decisions are likely to be affected only if the information in question is important to the specific decision being made.The overall financial statements are presented fairly	Material مهم
Disclaimer or Adverse تقرير عكسي	Most or all users, decisions based on the financial statements are likely to be significantly	High material مهم جدا

⁽¹⁾ Ibid, Arens, Alvin a. P.55

Official guidelines on quantitative measures of materiality

%5	%10)	%10- %5-1
		1%-%.5 -2
		%1 -3
		%1 - %.5 -4
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⁽²⁾Berger and Anthony CPAs

Materiality Guidelines

Professional judgement is to be used at all times in setting and applying materiality guidelines. As a general guidelines, the following policies are to be applied :

- 1- The combined total of misstatements in the financial statements exceeding 10 percent is normally considered material. A combined total of less than 5 percent is presumed to be immaterial in the absence of qualitative factors. Combined misstatements between 5 percent and 10 percent require the greatest amount of professional judgement to determine their materiality.
- 2- The 5 percent to 10 percent must be measured in relation to the appropriate base. Many times there is more than one bases to which misstatements should be combined. The following guides are recommended in selecting the appropriate bases:

⁽¹⁾ Ibid, William C.Boynton.P.226

⁽²⁾ Ibid, Arens, Alvin A .P.235

- a. Income statement. Combined misstatements in the income statement should ordinarily be measured at 5 percent to 10 percent of operating income before taxes. A guideline of 5 percent to 10 percent may be inappropriate in a year in which income is unusually large or small. When operating income in a given year is not considered representative, it is desirable to substitute as a base a more representative income measure. For example, average operating income for a 3-year period may be used as the base.
- b. Balance sheet. Combined misstatements in the balance sheet should originally be evaluated for current assets, current liabilities, and total assets. For current assets and current liabilities, the guidelines should be between 5 percent and 10 percent, applied in the same way as for the income statement. For total assets, the guidelines should be between 3 percent and 6 percent, applied in the same way as for the income statement.

3- Qualitative factors should be carefully evaluated on all audits. In many instances, they are more important than the guidelines applied to the income statement and balance sheet. The intended users of the financial statements and the nature of the information in the statements, including footnotes, must be carefully evaluated.

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Revenue recognition

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Elements of Financial Statements

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FASB

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" (CON 6)

Inflows or other enhancements of assets of an entity or settlements of its liabilities (or a combination of both) from delivery or producing goods, rendering services, or other activities that constitute the entities major or control operation (para. 78).

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Sales				
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Persuasive evidence of an arrangements exists.				-2
				-3
				-4
Collectability is reasonably assured				
:		Departure from the sale basis		-1
High degree of certainty				-2
Does not represent substantial completion of the earning process.				

: SFAC. No.3, Par 83

Recognition is “the process of formally recording or incorporating an item in the accounts and financial statements of any entity “

: SFAC.No.5, Par6

“Recognition includes depiction of an item in both words and numbers with the amount included in the totals of the financial statements, for an assets or liability, recognition involves recording not only acquisition or incurrence of the item, but also later change in it, including removal from the financial statement, previously recognized.

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1-Recognition

2-Realization

(SFAC No.3,Par.83)

Realization

“Realization is the process of converting noncash resources and rights into money and is most precisely used in accounting and financial reporting to refer to sales of assets for cash or claims to cash.”

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(Revenue recognition)

(Securities)

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(It is earned)

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Realized

Realizable

(Earned)

Revenue are earned when entity has substantially accomplished what is must do to be entitled to the benefits represented by the revenue, that is, when the earning process is complete or virtually complete .

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.Revenue recognition Classified by Nature of Transactions ⁽¹⁾

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Type of transaction			
Sale of asset other than inventory	Permitting use of an asset	Rendering a service	Sale of production from inventory
Description of revenue			
Gain or loss on disposition	Revenue from interest,rents,and royalties	Revenue from fees or services	Revenue from sale
Timing of revenue recognition			
Date of sale or trade-in	At time passes or assets are used	Services performed and billable	Date of sale (date of delivery)

⁽¹⁾ Ibid, Kieso, D. E .P.1002

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.⁽¹⁾ Transactions Approach

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All income and gains from whatever source derived	Total Income
	Mines (-)
Income excluded by law from taxation	Exclusion
Income subject to taxation(before deduction and exemptions)	Gross Income
	mines(-)
Generally business-related expense and losses according to Tax Law	Deductions to arrive at Adjusted gross Income
	Equals(=)
Significant because several subsequently deductible items are computed as or limited by some percentage of it	Adjusted Gross Income
	Mines(-)
The standard deduction or, in lieu thereof, itemized deductions allowed by law	Deductions from Adjusted Gross Income
	mines(-)
A deduction allowed by law	Personal Exemptions
	Equals(=)
Amounts to which appropriate tax are applied	Taxable Income

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After delivery		Before delivery			At date of delivery (point of sale)
After costs are recovered	As cash is collected	At completion of production	During production	Before production	The general rule

Special sales	
Consignments	Franchises

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SAS 1 (AU 110) states

The objective of the ordinary audit of financial statements by the independent auditor is the expression of an opinion on the fairness with which they present fairly in all material respects, financial positions, results of operations, and its cash flow in conformity with generally accepted accounting principles.

Practioneer

⁽¹⁾ Ibid, Kieso, D. E. P.1002

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Cycle Approach

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Cycles Approach Applied to XYZ Co.			
Income statement	Balance Sheet	Journals Included in the cycle	Cycles
Sales	Cash in bank	Sales Journal	(1) Sales and collection
Sales returns and allowances	Trade accounts receivable	Cash receipts journal	
Bad dept expense	Other accounts receivable	General journal	
	Allowance for uncollectable accounts		
Income statement accounts taken from General Ledger	Balance sheet accounts taken from General Ledger	Acquisition journal	(2)Acquisition and payment
		Cash disbursement journal	
		General journal	
Salaries and commissions	Cash in bank	Payroll journal	(3) Payroll and personnel
Sales payroll taxes	Accrued payroll	General journal	
Executive and office salaries	Accrued payroll taxes		
Administrative payroll taxes			

Cost of goods sold	Inventories	Acquisition journal	(4) Inventory and warehousing
		Sales journal	
		General journal	
Interest expense	Balance sheet accounts taken from General Ledger	Acquisition journal	(5) Capital acquisition and repayment
		Cash disbursement journal	
		General journal	

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	Accuracy (3)
	Classification (4)
	Timing (5)
	(6) Posting and summarization

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Analytical procedures defined by SAS 56 (Au 329) as evaluation of financial information made by a study of plausible relationships among financial and non informitional data, involving comparisions of recommended amounts to expectation developed by the auditor

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1- Tax avoidance: is the process of controlling your actions so as to avoid undesirable tax consrqences. It is a legal activity

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2- Tax evasion : is the illegal process of not complying with applicable provisions of the law once the transactions already exist

3- Tax planning: is the process of detecting the theoretical flaws in current tax authority in order to device transactions to make advantage of those flows⁽¹⁾ .

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⁽¹⁾ Steven J. Rice, **Introduction to Taxation**, South-Western Publishing Co. Cincinnati, Ohio.U.S.A.P.5

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“ The auditor should recognize that noncompliance by the entity with laws and regulation may materially affect the financial statements “.

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Representations

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“In the absence of evidence to the Contrary, the auditor is entitled to assume the entity is in compliance with these laws and regulations “.

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“The auditor does not test or perform at her procedures on the entity is compliance with laws and regulations since this would be out side the scope of an audit of financial statements”.⁽¹⁾

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**An-Najah National University
Faculty of Graduate Studies**

Audit for Tax Purposes

**Prepared by
Mohammad Mahmoud Theeb Husu**

**Supervised by
Dr. Hassan Falah Alhaj Mosa**

**Submitted in Partial Fulfillment of the Requirements for the Degree of
Master in Taxation Disputes, Faculty of Graduate Studies, at An-
Najah National University, Nablus, Palestine**

2005

Audit for Tax Purposes
Prepared by
Mohammad Mahmoud Theeb Husu
Supervised by
Dr. Hassan Falah Alhaj Mosa

Abstract

This research has been conducted to assure the importance of achieving Systematic Audit Approach. This can be achieved through studying the structural relationship between the Tax Systems and the Standards of different audit activities practiced currently in the economic units in Palestine.

The researcher has studied many literary writings related to audit and tax sciences in order to achieve his goal in establishing an active auditing system. He used the analytical reading approach in addition to analyzing system, making good use of his practical experience as an auditor in one hand and manager for more than one in Tax Departments in the Ministry of Finance in Palestine on the other hand.

The study results have shown that the success in managing Tax Units, stopping evasion and the falsification of accounts, do not lie only in punishing means written in Tax Laws or Professional Standards Institutions, but it lies in the well organized Tax Administration.

The study recommends the following:

- 1) The necessity of hastening the endorsement of suggested Palestine Income Tax and the serious thinking in changing the V.A.T law in a way that suits the specialties of Palestinian economic condition .
- 2) Harmonization between Tax Legislation and PSCPA in order to find lawful articles to punish those who work illegally.

- 3) The Tax Legislation should take care into accounts the principle of segregation of duties in tax process to ensure the neutrality and cleanliness in work, and applying the principle of accountability.
- 4) The Tax Administration should adopt the principle of historical reconciliation between the Palestinian traders and the tax responsables in order to remove the bad effects of the occupation.