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# *Introduction to Audit*

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**pwc**

# *Agenda*



*Introduction to Assurance*

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*Regulations, ethics*

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*Planning*

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*Questions*

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# *Introduction to Assurance*

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## ***Purpose of assurance services***

**The purpose of assurance services is to:**

***Increase the confidence***

***Reduce the risk***

***of the user of those services.***

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# *Elements of assurance engagement*

## **1. A three party relationship between**

- a practitioner (professional accountant - the auditor)
- a responsible party (preparer of the information)
- a intended user of the information

## **2. Subject matter**

## **3. Suitable criteria**

## **4. Sufficient appropriate evidence**

## **5. Written report**

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## *External audit*

The objective of an **external audit** engagement is to enable the auditor to express an opinion on whether the financial statements:

- Give a **true and fair view** (or present fairly in all **material respects**)
- Are prepared, in all material respects, **in accordance with an applicable financial reporting framework.**

## **Audit vs. Review**

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# *Materiality*

Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements.

## **True and fair view**

**‘True’** in accounting terms can be taken to mean **not factually incorrect**.

**‘Fair’** can have the following meanings:

- **Clear**
- **Unbiased**

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# *Limitations and benefits of statutory audits*

## **Benefits**

- High quality, reliable information circulates the market
- Independent verification
- Reduces the risk of management fraud and error

## **Limitations (why only reasonable assurance is provided)**

- Financial information includes subjective estimates and judgemental matters
- 100% of the transactions is not reviewed – sample basis testing



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## ***Expectation gap***

There is a common misconception about the role an auditor plays. This is often referred to as the 'expectations gap.'

### **Examples**

*a belief that auditors test 100% of transactions and balances*

*a belief that auditors are required to detect fraud*

*auditors are responsible for preparing the financial statements*

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# *Responsibilities*

## **Management's responsibilities**

Management are responsible for ensuring the entity complies with relevant laws and regulations.

This means:

- **monitoring** of legal requirements,
- **development** of systems of internal control (to ensure compliance)
- an effective system of **assessing the effectiveness** of those control systems.

## **Auditor's responsibilities**

The auditor is responsible for obtaining reasonable assurance that the financial statements are free from material misstatement.

# *Regulations, ethics*

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# ***ISA***

## **International standards on auditing (ISAs)**

- There are currently 36 ISAs
- All audits carried out under the laws of member states of the EU have had to be conducted under ISAs for all accounting periods beginning on or after 1 January 2005.

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# ***Criteria for statutory audit applicable in the Czech Republic***

**Kritéria** pro povinný audit řádných a mimořádných účetních závěrek, dle §20 zákona o účetnictví od **1. 1. 2016**

## **Dle § 20 jsou povinně auditovanými jednotkami:**

- velké účetní jednotky s výjimkou vybraných účetních jednotek, které nejsou subjekty veřejného zájmu
- střední účetní jednotky
- malé účetní jednotky, pokud jsou akciovými společnostmi nebo svěřeneckými fondy a překročily nebo dosáhly alespoň 1 ze 3 zákonných (níže uvedených) kritérií za aktuální účetní období a za období bezprostředně předcházející
  1. Aktiva celkem 40 mil. Kč (nově je třeba však brát aktiva v netto nikoliv v brutto hodnotě)
  2. Úhrn čistého obratu 80 mil. Kč
  3. Průměrný přepočtený počet zaměstnanců 50
- ostatní malé účetní jednotky, pokud překročí nebo dosáhnou alespoň 2 ze 3 zákonných kritérií za aktuální účetní období a za období bezprostředně předcházející

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## *Description of categories since 1 January 2016*

### **Kategorizace účetních jednotek od 1. 1. 2016**

- **mikro účetní jednotka** (nepřekračuje alespoň dvě z těchto hraničních hodnot – 9 mil. Kč aktiva celkem, 18 mil. Kč roční úhrn čistého obratu, 10 průměrný počet zaměstnanců)
- **malá účetní jednotka** (není mikro účetní jednotkou a nepřekračuje alespoň dvě z těchto hraničních hodnot – 100 mil. Kč aktiva celkem, 200 mil. Kč roční úhrn čistého obratu, 50 průměrný počet zaměstnanců)
- **střední účetní jednotka** (není mikro ani malou účetní jednotkou a nepřekračuje alespoň dvě z těchto hraničních hodnot – 500 mil. Kč aktiva celkem, 1 mld. Kč roční úhrn čistého obratu, 250 průměrný počet zaměstnanců)
- **velká účetní jednotka** (překračuje alespoň dvě z těchto hraničních hodnot – 500 mil. Kč aktiva celkem, 1 mld. Kč roční úhrn čistého obratu, 250 průměrný počet zaměstnanců).

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# *Appointment and removal of auditor*

## **Who appoints the auditor and how long for?**

- The **shareholders** of the company by voting them in at the Annual General Meeting (AGM)
- Generally, appointment runs from the end of the AGM until the end of the next AGM.

## **Removing the auditor**

- majority at a general meeting
- resignation

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## *The Auditor's rights*

- Access to the company's books and records.
- To receive information and explanations necessary for the audit.
- To receive notice of and attend any general meeting of members of the company.
- To receive copies of any written resolutions of the Company



# *Fundamental principles, threats and safeguards*

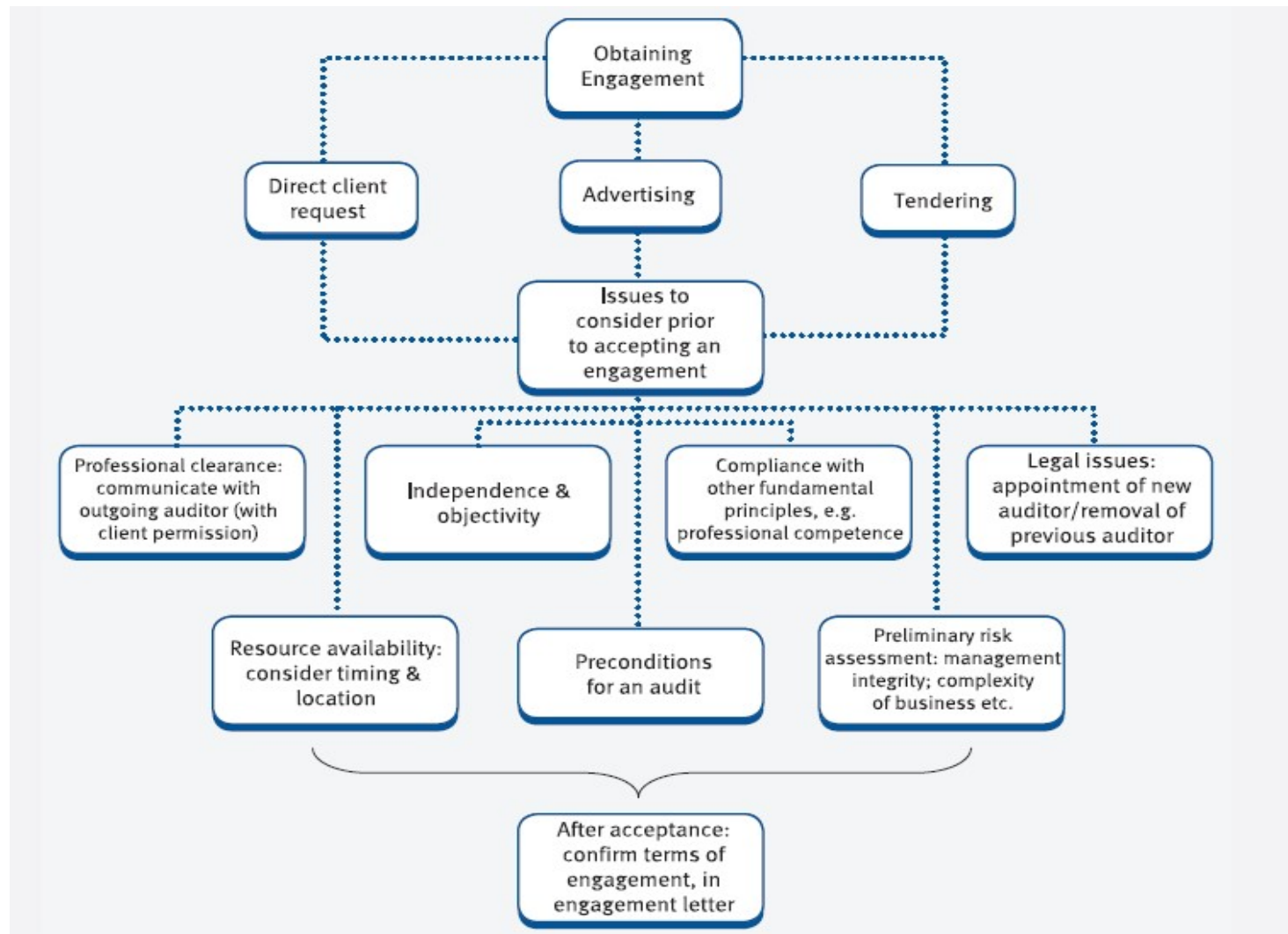
## Fundamental principles, threats and safeguards

**FUNDAMENTAL PRINCIPLES**  
Integrity  
Objectivity  
Professional competence and due care  
Confidentiality  
Professional behaviour

**THREATS**  
Self-interest  
Self-review  
Advocacy  
Familiarity  
Intimidation

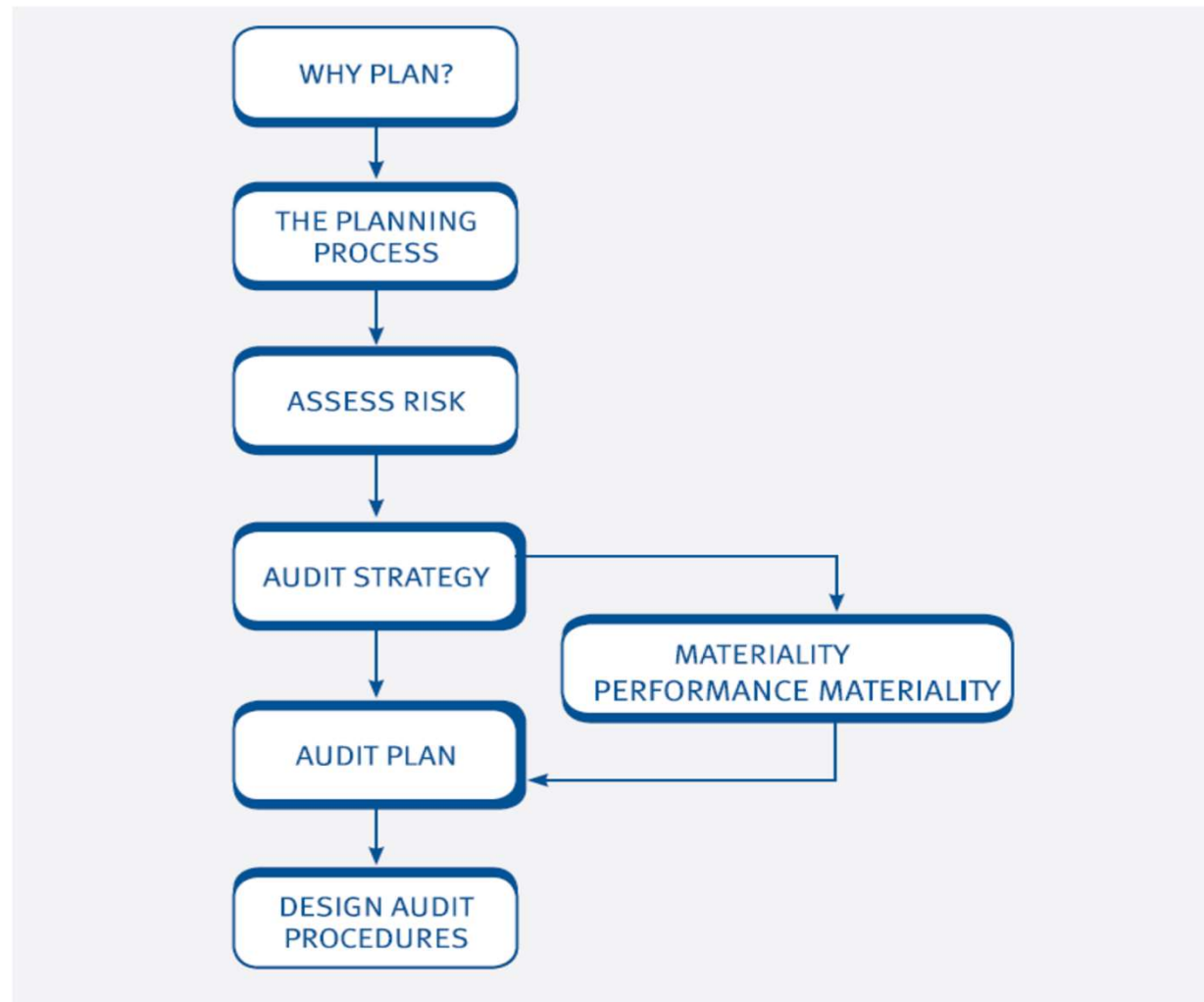
**SAFEGUARDS**  
**General**  
Created by the profession  
Created by individuals in the work environment  
**Specific**  
Segregation of duties  
Review  
Rotation  
Ceasing to act

# Acceptance process



# *Planning*

# *Planning process diagram*



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# *The planning process*

## **Preliminary engagement activities**

- Evaluating compliance with ethical requirements
- Establishing the terms of the engagement

## **Planning activities**

- Developing the **audit strategy**
- Developing an **audit plan**
- Design **audit procedures**: Planning the nature, timing and extent of direction and supervision and the review of work

# *Audit risk*



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# ***Materiality***

‘Misstatement, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements’.

## **How is Materiality Determined**

- **Common measures are:**
  - ❑ 1/2 – 1% of turnover/revenue
  - ❑ 5 – 10% of profit before tax
  - ❑ 1 – 2% of gross assets
- **Overall materiality**
- **Performance materiality**

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## *Definition*

**An item can be material:**

**By  
size**

*Huge amount of money*

**By  
nature**

*amount is not relevant, indicates future developments  
or other significant events whose disclosure is  
compulsory*



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## ***Fraud and error***

### **Misstatement in the financial statements can arise either from**

- **Fraud** – an **intentional** act involving the use of deception to obtain an unjust or illegal advantage
- **Error** – an **unintentional** mistake and could include accidental misapplication of accounting policies or oversights

**Fraud is a criminal activity** but it's not the role of the auditor to determine whether fraud has actually occurred. That's responsibility of a country's legal system.

# *Questions?*

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***Thank you for your attention.***

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