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E-mail id: saarjjournal@gmail.com

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CONCEPT OF IMPORTANCE IN AUDIT PLANNING AND EXECUTION

Ismanov I.N.*; Mo'ydinov E.D**

*Professor,
Doctor of Economics,
Head of the Department of Accounting and Audit,
Fergana Polytechnic Institute, UZBEKISTAN

**PhD in Economics, Associate Professor,
Chief Auditor of "PROFI AUDIT",
UZBEKISTAN

ABSTRACT

This article defines "materiality" based on international auditing standards.The procedure for planning, conducting and using this concept in the audit process has been completed.In addition, the concept of "materiality" and the impact of "audit risk" on the "audit report" presented to the client at the end of the audit were considered on the basis of the opinions of leading scientists in the field of an international audit.

KEYWORDS: *Audit Risk, Auditor's Working Paper, Distorted Readings, Fraud, Inductive Method, Internal Control, International Auditing Standards, Main Indicator, Mistake, Persons Entrusted With The Functions Of Administration, Policy Account, Professional Review, Risk Management System Tools, Risk Not Being Able To Identify, The Deductive Method, Uncorrected Distortions, Users Of Financial Statements, Value.*

INTRODUCTION

Assessing the level of "materiality" is one of the most important issues in the theory and practice of international audit. This direction is described in detail in the International Audit Standard No. 200 (IAS) "General Goals of an Independent Auditor and the Conduct of Audits in Accordance with International Audit Standards" and IAS No. 320 "Importance in the Planning and Conduct of Audits."In a number of other IAS, there are also cases where this problem is solved.The IAS 450 standard "Assessment of violations identified in the audit process" sets out the procedure for applying the materiality criterion when assessing the impact of identified violations on the audit and non-eliminated violations (if any) in the financial statements.

RESEARCH METHODS

The term "materiality" means the highest value of distortion of financial statements, from which a qualified user of this report will no longer be able to draw correct conclusions and make correct decisions based on it.

The overall objective of the auditor who conducts the audits on the basis of which the ISAs are considered is to:

– It is reasonable to ensure that financial statements generally do not contain material misrepresentations due to fraud or error;
– proper application of the concept of materiality in audit planning and execution;
– Assess the impact of identified violations on the audit and the impact of uncorrected violations (if any) on the financial statements.

The term "error" is used to describe intentional misstatements and circumstances that occur in financial statements.

For example, distortions can result from:

a) errors (inaccuracies) in the collection or processing of information, which is the basis for the preparation of financial statements;

b) withholding any amount or disclosure;

c) inaccuracy of the estimated estimate made as a result of omission or misinterpretation of reality; and

d) judgments of the management of the enterprise that the auditor considers unreasonable or that the auditor considers the accounting policy inappropriate.

The definition of "fraud" is set out in ISA 240 "Duties of the auditor for fraud in the audit of financial statements." [2]

According to him, fraud is a deliberate act committed by one or more persons from among the leadership, persons entrusted with management, employees or third parties in order to obtain unfair or illegal benefits by deception.

According to the current legislation of the Republic of Uzbekistan, its head is responsible for the correctness of accounting at enterprises, regardless of the form of management and form of ownership, as well as for ensuring the reliability of reports submitted.

In particular, according to article 11 of the Accounting Act, entitled "Organization of accounting and reporting," the organization of accounting and reporting is carried out by the head of accounting. Head of Accounting:

– development of accounting policy, a system of internal accounting and reporting;

– internal control procedures;

– complete and reliable accounting;

– the integrity of accounting documents;

– Preparation of financial statements;

– Preparation of tax reports and other financial documents;

– ensure timely calculations.

RESULTS AND DISCUSSION

To prevent significant errors in financial reporting as a result of "errors" and "fraud," the company's management must create an effective internal control system.Internal control is organized on the basis of the accounting policy adopted by the head of the accounting entity in order to ensure the legality, economic expediency, the safety of assets, prevention and detection of robberies and errors in accounting, financial and other statements; this is a system of measures taken.The correctness of the internal control system, its complexity, the involvement of knowledgeable and qualified specialists, its provision with modern technical means of control, as well as the effectiveness of the system timely detect errors and fraud in the enterprise. enables the development of preventive measures.However, audit practice shows that no matter how effective an internal control system is, there is still a possibility that damaged data will be reported as a result of errors and fraud.With this in mind, before the auditor initiates an audit, the client determines the appropriate audit procedures to assess the state of the entity's internal control system and thus determines the level of trust in the information provided for the audit.In accordance with paragraph 4 of IAS 320, the auditor's determination of materiality is a matter of professional judgment and will depend on the auditor's understanding of users' need for financial information from financial statements.In this context, the auditor has reason to assume the following about users:

a) They have knowledge of business, economic activities and accounting, and have reasonable diligence to study the information provided in the financial statements;

b) they understand that financial statements are prepared, presented and verified based on their materiality;

c) they recognize that estimates of amounts based on the use of estimates, consideration and consideration of future events are uncertain;

d) make sound economic decisions on the basis of information provided in the financial statements.

In audit practice, the materiality threshold is set to reduce to a reasonable level the probability that the amount of unadjusted and undetected distortions in financial statements may exceed the level of materiality.As noted above, the concept of materiality is used by the auditor when planning, conducting and completing an audit, that is, when assessing the impact of identified violations on the audit report and financial statements for uncorrected violations (if any).Audit planning involves defining an overall audit strategy and developing an audit plan for an audit assignment.

Therefore, the auditor must determine the materiality of the financial statements of a particular business entity when determining the overall strategy of the expected audit and when developing an audit plan.The value can be evaluated in terms of both quality and quantity. When assessing the quality of the identified deficiencies, this deviation is considered a "significant" or "insignificant" event in terms of how the legislation differs from the accounting for these transactions, that is, the nature of the violation and its impact on the accuracy of financial statements.

For example, a qualitative assessment of materiality can be applied to the following circumstances that can be identified during an audit:

– the existence of a accounting policy or the inconsistency of the circumstances reflected in it;

– non-disclosure as required by law and the International Financial Reporting Standards (IFRS);

– Failure to perform an assessment supporting the validity of the business continuity assumption or the low level of credibility of such an assessment, etc.

When the level of materiality is quantified as described in paragraph 2 of IFRS 320, distortions, including omissions, if they occur on their own or in conjunction with other distortions, reasonably relate to economic decisions made by users based on financial statements. The degree of exposure has been studied.When determining the validity of materiality, the auditor must distinguish for himself the materiality of the financial statements of the enterprise, which is expected to be checked.At the same time, he can use the following methods, which are sufficiently disclosed in the theory of audit and are used in practice. (Table 1.)

TABLE 1. THE METHODS USED TO IDENTIFY SIGNIFICANT INDICATORS ALLOW YOU TO CALCULATE THE LEVEL OF SIGNIFICANCE.

Extremely careful method of substances	Stable Performance Method	Basic Array Method	Method of at-risk indicators	The result is an important indicator method

1. The OTC position method is based on the selection of key figures that financial reporting users can focus on first.For example, in joint-stock companies the indicator "Profit per share."
2. The method of stable indicators selects indicators that are not subject to significant changes during the reporting period.For example, authorized capital, final financial statement value, long-term assets.
3. When selecting key figures in the main array method, their share in the total value of financial statements is taken into account.That is, in this method, indicators with a large proportion are significant.
4. Reporting elements with a high error rate compared to other indicators should be selected in the method of at-risk indicators.
5. The method of significant indicators should take into account indicators that the presence of errors and deviations can lead to significant consequences associated with the violation.

In audit practice, the procedure for their application in combination is generally accepted.

In accordance with paragraph A4 of IFRS 320, the income categories reflected in the reports, in particular, profit before tax, gross operating income, gross profit and total expenses, total capital or assets, are examples of indicators that can be considered acceptable depending on the circumstances of the business entity, net worth can be quoted.

US professors Arens E.A., Lobbeck Dj. K. consider it appropriate to divide the use of the concept of "materiality" in audit practice into five stages (3.231b):

1. Define the initial overall significance level (s);

2. Distribute the initial overall level of materiality among the reporting elements;
3. Determination of the fair value of financial statements for individual items;
4. Determination of the total fair value of the level of materiality in the financial statements;
5. Compare the actual significance level to its original value.

The first stage. Determining the initial overall significance level (value). At this stage, the auditor determines the minimum (minimum) and maximum (maximum) limits of possible errors.Errors below the minimum limit were considered minor errors, and the auditor did not consider it necessary to pay much attention to their study.Errors above the maximum limit are significant errors and should be thoroughly investigated by the auditor as they may adversely affect the accuracy of financial statements.The determination of the percentage to be applied to the selected target implies the professional opinion of the auditor. Professor J. Robertson writes that most auditors consider errors in the range of 5-10 per cent as minor, minor errors.Errors exceeding 10 per cent are classified as significant errors [7].

The following indicators and quantities can be used to determine the level of minor deviations in audit practice [6].

- annual net profit - up to 5%;
- from net profit - up to 2%;
- from financial statement currency - up to 2%
- from the value of private capital - up to 10%;
- from total expenses - up to 2%.

Indicators adapted to determine the level of importance in different industries and their percentage level may differ. For example,

- an article for the oil and gas industry that may be added or replaced by any of the above indicators - the cost of fixed assets;
- for freight transport organizations - the volume of transported goods;
- for trading enterprises - turnover;
- for investment organizations - profit before tax.

The value can be calculated based on two different approaches:

- deductive;
- inductive.

The deductive approach first determines the level of the materiality of the financial statements be audited and then distributes this value to the materiality items of the financial statements.

In an inductive approach, the levels of materiality in financial statements are first determined by the items of materiality, and then the total level of materiality in financial statements is determined as their amount.According to Professor J. Robertson, the deductive method is theoretically more suitable for assessing materiality [7].

Significance is calculated separately for each client, taking into account the results of their previous audits, the characteristics of the business, the level of trust in it in the business community and a number of other factors, and this is documented in the corresponding working document of the auditor.Here is an example of calculating the significance level in a deductive way.(Table 2.)

TABLE 2. CALCULATIONS TO DETERMINE THE SIGNIFICANCE LEVEL BASED ON A DEDUCTIVE APPROACH.

Keyindicators	The sum of the main indicator, thousand soums	Estimated level of significance, %	Acceptable amount for determining the level of importance, thousand soums	Share, %
1	**2**	**3**	**4**	**5**
Netincome	7 800 500	0,50%	39 003	18
Annualnetprofit	960 300	4,00%	38 412	18
Grossexpenditure	6 840 200	0,50%	34 201	16
Financialpositionreportingcurrency	12 657 890	0,50%	63 289	29
Privatecapital	4 369 752	1,00%	43 698	20
Intotal	**32 628 642**	**x**	**218 602**	**100**

1 option. In this case, the single significance level for all key figures is taken as the amount is shown in row 3 of Table 1 - 34,201 thousand. Soum, which can be rounded more (35,000 thousand Sumov) or less (34,000 thousand Sumov) in order to reduce practical benefits. In this case:

– rounding in the direction of multiplication (35,000,-,34,201,)/34 201 * 100% = 2.34%
– round down (34,201,-,34,000,)/34 201 * 100% = 0.59%

In audit practice, a deviation of up to 20% is considered acceptable, and if it is exceeded, the auditor needs to take additional measures to regulate settlements. As we see, the percentage of deviation is small in both cases. Therefore, the selected amount (34,000 thousand Sumov) is considered as the level of general significance for all main indicators. At the same time, the level of materiality for all financial statements (34,000 thousand.Sumov * 5) is set at 170,000 thousand. Soum. This amount represents 1.34% of the total cost of the statement of financial position (170 000/12 657 890 * 100), and this figure is below the level recommended in audit practice (5-10%), to the satisfaction of the audit organization.

2 option. In that case

a) Based on the data in column 4 of Table 1, we calculate the average significance level (39 003 + 38 412 + 34 201 + 63 289 + 43 698)/5 = 43 721 thousand Sumov

b) values of indicators that differ more or less by an average significance level are excluded from the set. In our example, these amounts are 63.289 thousand. Sumov and 34,201 sum.

c) the new average value is determined based on the remaining values (39,003,+,38,412,+,43,698,)/5 = 40,371 thousand Soum

d) rounded to the side for ease of use. Then, according to our example, the total level of significance for all main indicators will be 40,000 thousand sums, and the level of significance for the total financial report (40,000 thousand sums * 5) will be 200,000 thousand sums. This amount represents 1.58% of the total cost of the financial statement (200 000/12 657 890 * 100), which is less than the level recommended in audit practice (5-10%) to the satisfaction of the audit organization.

There are several advantages of the method of determining the level of materiality by the average value of the baseline indicators. Including:

- Changing key indicators, removing some or introducing new ones;
- Change the proportion of key indicators based on their knowledge and experience;
- change the rounding order;
- Taking into account the indicators of the previous year and the pace of their change;
- Applying different levels of significance to the reporting elements and individual elements of the main indicators;
- Development of a table for calculating the significance level and a specific methodology for calculating its level.

The second stage. Distribute the initial overall materiality level among the reporting elements. At this stage, the auditor distributes the initial overall level of materiality among the items in the report.

We will explain this by dividing the initial level of importance (34,000 thousand Sum), defined by the Private Equity Index, into individual elements.

TABLE 3. THE ORDER OF DISTRIBUTION OF THE VALUE OF THE ORIGINAL SIGNIFICANCE, DETERMINED BY THE MEASURE OF FAIRNESS, AMONG ITS ELEMENTS.

The title of the articles of private capital	The amount, thousand sums	Share,%	Distribution of value, thousand sum
Authorized capital	1 000 000	22,89%	7 780
Added capital	580 000	13,27%	4 513
Reserve capital	360 950	8,26%	2 808
Retained earnings	1 308 802	29,95%	10 184
Target financing	1 120 000	25,63%	8 715
Total	**4 369 752**	**100,00%**	**34 000**

Similarly, the only value that is taken into account for other financial reporting indicators is distributed among the components.Based on this information, the auditor will have preliminary information on the weaknesses of the financial statements that are expected to be audited, and these circumstances will be taken into account in the preparation of the audit plan.

The third stage. Determine the actual value of the importance of financial reporting for individual items. At this stage, the auditor calculates the amount (H) of errors actually made for each item involved in the financial statements.If the sum of the actual error is determined using a sample, then for this article the sum of the actual error is divided by the sum (A), the total value of the tested self-calculations - by the sum (c) multiplied by the total amount of the set (C).

$$X = (A/B)*C, \quad (1)$$

Example: During the audit, the following information was obtained under the heading "Reserve capital" of private capital.

A = 1,800,000 soums

V = 178 500 000 soums

S = 200 210 thousand Soum

Solution: X = (A/B) * C = (1 800/178 500) * 200 210 = 2,018 thousand. Soum

It turned out that the actual amount of error under the reserve capital item of the Private Equity Index adapted to determine the level of materiality is 2,018,000 soums.This is 790,000 sums less than the originally planned level (2,808,000 sums).Thus, the fair value of distortions for other indicators and their items is determined to determine the initial level of materiality in the financial statements.Assuming that when performing these calculations for other items of the Private Equity indicator, based on the results of their audit, the actual amount of errors was as follows.

- Authorized capital-1 200 thousand soums;
- Added capital - 5,956 thousand soums;
- Retained earnings - 11 830 thousand soums;
- Earmarked financing - 9,934 thousand soums;

Stage 4. Determine the overall actual value of the importance of financial reporting. At this stage, we expect the overall level of remuneration for the level of importance in the general financial statements.

See 1,200 + 5,956 + 2,018 + 11,860 + 9,934 = 30,968 thousand soums.

Stage 5. Compare the actual significance level to its original value. At this stage, as a result of the audit, the amounts of errors detected in fact for all items of the baseline indicators are compared with their initial values and a corresponding working document is compiled.

We explain this process by implementing it in accordance with the articles of the basic indicator "private capital."

TABLE 4. COMPARISON OF THE LEVEL OF SIGNIFICANCE DETERMINED IN REALITY BY THE BASIC INDICATOR OF PRIVATE CAPITAL WITH ITS INITIAL LEVEL.

The title of the articles of private capital	Initial significance level, thousand soum	Level of real importance, thousand soum	Amount ofdifference,thousand soums
Authorized capital	7 780	1 200	- 6 580
Added capital	4 513	5 956	1 443
Reserve capital	2 808	2 018	- 790
Retained earnings	10 184	11 860	1 676
Target financing	8 715	9 934	1 219
Total	**34 000**	**30 968**	**3 032**

As can be seen from the data of Table 3, according to the audit results, there was a difference in both the decrease and the increase in all points of the investigated indicator.

In this case, the auditor's response to the actual distortion is set out in paragraph 6 of ISA 400 "Evaluation of control detected during the audit."

According to him: The auditor should determine whether it is necessary to revise the overall audit strategy and audit plan if:

a) the nature of the revealed violations and the reasons for their occurrence indicates that there may be other violations that may be significant in the totality of violations collected during the audit; or
b) the number of violations accumulated during the audit reached the level of materiality determined in accordance with ISA 320.

The auditor shall review the initial level of materiality if it is determined that the financial results actually achieved at the end of the period are likely to differ significantly from the financial results used to determine the level of materiality originally expected for the financial statements. This may lead to a revision of the overall audit strategy and audit plan. In this case, an audit working paper should be prepared. This is because article 14 of ISA 320 sets out the circumstances under which the relevant audit documentation on materiality based on ISA 230, entitled "Audit Documents," should be prepared. In particular, the Auditor shall include in the audit documentation the following amounts, as well as the factors taken into account in determining these amounts:

a) level of significance for financial reporting;
b) where appropriate, the level of importance of transactions, account balances or certain categories of disclosures;
c) significance limit;
d) (g) Revise paragraphs (a) to (c) by any means, depending on the results of the audit.

The auditor shall promptly notify the management of the business entity of any violations identified during the audit.At the same time, when presenting the identified circumstances to the management of the enterprise, the auditor must ask the management of the business entity to correct such violations and, after correction, notify the auditor in writing about each corrected and unadjusted value of each of the indicators.In some cases, the management of the business entity and, if necessary, persons with managerial powers may consider that some uncorrected distorted information is not distorted information.They may, therefore, add the following words to the definition of their written statement: “We do not agree that the articles... and... are a distortion because [description of causes]”.However, receiving such a notice does not relieve the auditor of the need to describe the conclusion about the consequences of uncorrected violations. [2]

If the management of the organization refuses to correct all or some of the violations reported by the auditor, the auditor must determine the reasons why the management of the organization does not correct the violations and take this into account when assessing the presence of significant distortions in the financial statements.As we see, there is a direct relationship between the level of materiality and audit risk.However, these relationships are inverse.That is, the higher the level of materiality, the lower the audit risk, and vice versa, the lower the level of materiality, the higher the level of audit risk.This means that if the auditor concludes that the inconsistencies identified in the audit require revision to reduce the initial level of materiality, it means that the audit risk should be reviewed at the initial level.In this case, audit practice recommends the use of one or both of two methods to reduce the level of audit risk.According to the first method, additional audit procedures should be used to reduce the level of risk of controls and the risk of their inability to detect by changing the colour, duration and size of tests to be performed.The second method is to address the significant irregularities identified by the management of the enterprise before the audit report is published and to ensure that the financial statements are resubmitted.Finally, the level of materiality directly affects the audit opinion, which is presented to the audited entity at the end of the audit.This relationship can be seen in the following diagram.

5 - TABLE. RELATIONSHIP BETWEEN MATERIALITY AND AUDIT OPINION.

Degree of importance	The importance of user decision-making	Form of conclusion
Doesn’t matter	Uncertainty does not affect decision-making	Positive feedback
For some substances is important	Uncertainty affects the user's decision only if this undefined information depends on the nature of the decision being made. In general, financial statements are considered to reflect reliable data	With comments
Important for most substances	Uncertainty affects most of the decisions made by the user based on these financial statements	Negative
	Inability to collect sufficient audit evidence as a result of limited audit scope	Refusal to conclude

CONCLUSION

In conclusion, determining the initial level of materiality in the process of planning an audit based on the ISA and making the necessary adjustments to it during the audit, as well as providing the client with an audit opinion based on the results of assessing the actual level of materiality.

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