

Risks of material misstatement

Business



The paper "Risks of Material Misstatement" is an outstanding example of an assignment on business. The purpose of this memo is to highlight the main elements of AU section 314, Understanding the Entity and Its Environment and Assessing the Risk of Material Misstatement which is made effective for audits carried out for periods beginning on or after December 15, 2006. The purpose of AU 314 is to provide strict guidelines and support for auditors to understand the levels of risks associated with their audit engagements. Auditors are required to develop sufficient understanding of the entity business and its internal controls in order to assess the risk of material errors and omissions in the financial statements so that incidences of misstatements or fraud can be avoided. In this way, auditors can evaluate and decide the nature, timing, and extent of audit procedures to be conducted (FASB, 2006). This suggests that auditors need to obtain an understanding of the internal controls which are already in place within the organizational structure in order to assess their efficiency and effectiveness and decide whether substantive testing is required to be developed and implemented. The standard provides details of procedures which auditors need to carry out for their assessment. The guidelines provided in this standard also cover the documentation which auditors need to make upon an assessment of the entity and its environment. This standard needs to be applied in conjunction with other auditing standards including AU 312, AU 326 and AU 318 which provide further guidance on assessing the materialism related to the existence of risks and procedures to be adopted by auditors in light of the assessed levels of risk (FASB, 2006). Thus, AU 314 provides guidelines for a risk-based approach to auditing by providing guidelines for assessing business risks and control risks that may exist within

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the organizational environment so that auditors can plan out their activities accordingly.