

# Analyze and evaluate the system of internal control in the process of implementing the audit of financial statements for business entities

Pece Nikoloski, Goce Menkinoski,

*Faculty of economics in Prilep, Macedonia*

E-mails: *nikoloski.pece@yahoo.com, gocemenkinoski@yahoo.com*

## Abstract

Accounting is the process of recording, classifying, summarizing and reporting results from financial transactions in the form of financial statements. Other than accounting, auditing the financial statements determines whether those statements are prepared in accordance with generally accepted accounting standards. You could say that this kind of audit users of financial statements provides objective and independent opinion on the truthfulness and honesty of the data presented in financial statements of business entities that are clients. The application of the system of internal control in the implementation of the audit process is very important activity in the process of making business decisions to allocate economic resources and successful management. Information obtained from the analysis answer the question as business entity in the previous period and how to function in the next period to be maintained better result. The main goal of any business entity is achieving greater profits. The profit maximization is striving to achieve the possible cost less and also the achievement of greater revenues. Profit shown in the financial statements may differ from reality depending on the way you handled the financial statements or in other words the way reports display where they can be concealed large gains and losses. From there the auditors are those who weigh the reality of participants' data in financial reports. How the financial result is a real set, so will be better and better decisions are made based on such information. The advantages of better financial reporting are significant, hence the actions needed to achieve those benefits are complex and comprehensive. As such we list the following activities: improving the framework of financial reporting; strengthening of key factors within the financial reporting; supporting the audit profession; supporting education, training and public awareness. The main and primary objective of financial reporting is to provide access balanced between financial reporting and audit requirements, which means meeting the needs of different users of financial information but also will be complex to burden the functioning of the corporate sector. In practice, here are three main reasons to perform the process of analyzing financial statements and financial indicators achieved:

1. The need for continuous monitoring of their own situation analyzes achieved financial indicators, financial instruments are planned and implemented financial control;

2. Calculation and analysis of financial indicators of business partners with whom the business entity enters into a variety of business relationships;
3. When investing in securities to thoroughly check the solvency of the issuer of the securities or of potential investors to provide all relevant information for making decisions about investing in capital to protect against possible speculative things.

**Keywords:** Accounting, system, Analyze, process, financial statements , Information, financial reporting

## 1.INTRODUCTION

The word "audit" etymologically derives from the Latin verb "revidere" which means "to examine" and the word "revisio" meaning "re-examine" or "to see". In English-speaking audit used the term "audit", which originates from the Latin word "audire" which means "hear". Auditor (auditor) in the English language is "one who listens" and from there comes the term audit (audit) which until today has retained its original form. In Germany, the audit used the word "Wirtschaftsprüfung", and the term "revision" as used in France "revision" and "revision compatible" and. t. slightly.

The review of the literature identified a "spiritual repetition of activities" which indicates its character as a function of checking the operation. Specifically, the audit is further verification of the implemented business events, which is based on existing documents, as opposed to control mainly a corrective nature.

In this regard Tom Lee, one of the most respected scholars in the field of auditing in the world in the early eighties, that in 1984 has given one of the best definitions of the term "audit" which reads: "In the broadest sense, the audit means by which a person assures (by another person) in the quality, condition or status of a subject matter that the other person examined. The need for testing arises because the person is in doubt or questioning the quality, condition or status of the relevant subject matter and is unable to remove such opinion or dilemma. "

Unlike the quoted definition of Tom Lee, which is undoubtedly concise, logical, and wide enough for clarification of different more types of revision. Committee of the American Association of Accountants, (American Association-AAA), defines audit as "a systematic process of objectively collect and evaluate evidence relating to reports on economic developments and results to verify the extent between existing reports operation and criteria and distributed to interested parties. "

Seen from the picture we notice that the audit itself is not a simple process, is rather complicated and complex process, with clearly defined objectives, based on which defines and structures the approach to making business decisions. The audit considered as systemic process involves collecting and objectively evaluating evidence. Consequently, the evidence present information that have great influence in making business decisions by the auditors. But regardless of the form appearing on the evidence and their reliable power, the auditor is required to precisely define the objectives of the process of collecting and evaluating relevant evidence.

During the process of implementation of the audit, the auditor receives as input financial statement of the business entity of the audit, which should thoroughly check and based on tests conducted formed and expressed an expert, objective and independent opinion. During the implementation of the review procedure, the primary objective of the auditor is

to determine whether the statements of the entities to audit with established criteria, usually associated with certain rules prescribed by the legislative body, plan or other measures of performance determined by management, accounting standards or other authoritative bodies.

The goal will be achieved and realized if the auditor gather evidence of economic developments and results to determine whether they adequately presented in accordance with established criteria, prior to distributing the results of operations of the client to potential stakeholders.

Similar views on the revision of the AAA provides renowned professional association of Great Britain, the Monitoring Committee of the audit practice gives the following definition of the audit: "An audit is an independent examination and giving-expression of opinion on the financial statements of companies, banks or other organizations by the appointed auditor, which is made in accordance with the requirements of the set task and the appropriate legal and professional obligations, or appropriate regulations. "

When it comes to defining the audit by the professional associations to build a reputation in the world, special attention deserves the definition of IFAC, by which the audit is an independent examination of financial statements or financial information to those that apply to profit-oriented entity or regardless of its size or legal form, when such testing is encouraged in order to express an opinion on them. "

If you try to make parallels between the cited definitions, it is safe to conclude that all of them immanent it contains mainly a few key words and phrases such as: independence, investigation, expression, opinion, person-authorized auditor and the like. . . From which each word individually in a strictly defined place and is indispensable for the precise formulation of the external audit. Thus, the term independent indicates that the auditor must be completely independent in terms of client with whom we conduct an audit, and his independent opinion to be accentuated as credible and fair for the users of audit services (shareholders, creditors, depositors, potential investors, government authorities, government agencies, etc.). independence of the auditor based on the fact that the audit must be independent and this in terms of company and in relation to the state, banks and all users of audit services, which has as a goal to protect public interests, the interests of capital owners - the shareholders, the government, investors, creditors, or any owner of a loyal citizen of a particular country. The word examination of the financial statements indicates that the audit joins generally accepted rules and techniques which determines the efficiency and integrity of the control system as well as accuracy, precision, completeness of the accounting statements in order to enable the auditor to establish its opinion. Competent opinion is that the auditor, even when a given event expresses a positive opinion about the reality and objectivity of financial reports presented to the company (client), in principle, does not guarantee the absolute accuracy of audited statements, but merely gives its opinion. Expression of opinion must be expressed in the form of a written report in accordance with Article 47 of the Fourth Directive of the European Union, is an integral, t. is. integral part of the annual calculation and with it a subject of public publishing. Under auditor means a competent and professional person who is appointed on a regular and orderly manner in accordance with criteria stipulated by laws and procedures to educate and appointment. Bearing in mind the basic objective of the audit with which increasing responsibility in the company's operations and its economic efficiency, its role can be viewed as: social, economic, psychological, public or personal interest.

## **2. An audit of financial statements (Financial Statements Audits)**

Audited financial statements as it aims to provide independent and objective opinion on the truthfulness and honesty of the data presented in the financial statements of companies. The focus of interest in the audit of financial statements, mostly basic financial statements: balance sheet, income statement and a statement of cash flows. Are these statements are made with generally accepted accounting standards, auditing of financial reports has the task to determine. In this direction, stressing the essential role of real and fair presentation of financial statements in all process of making business decisions makers MRS through the purpose and content of these standards are explicit in insisting that the financial statements of business entities need to be prepared in combination or in accordance with one of the following standards:

- International accounting standards;
- National accounting standards;
- Other established and agreed framework of financial reporting

## **3. The review of compliance procedures**

The review of compliance procedures for its aims to determine the extent to which business entity in which the audit is performed following the standards or rules-established, adopted or created by the higher levels contracts, legislation or written consent. Under higher levels authoritative means top management that commits the standards of certain areas of its operations to incorporate the policy actions of the business entity in the preparation of specific guidelines and instructions. In practice, revision of compliance focuses only on examining the standardization of procedures on a separate set of standards and rules. In such cases, the auditor seeks to see deviations from the procedures prescribed rules and standards and in time to inform top management about perceived condition. Thus, revision of compliance has the following features:

- The company engages auditors and to determine the area of auditing, along with the presentation of standards relevant to that area of operation of the business entity;
- Auditor's report to top management of the business entity for its activities and information, which came during the audit.

### **3.1. Review of operations**

The audit of operations targeting has to perform a systematic examination of the activities of the business entity or part thereof, in terms of effective and efficient use of resources. Examining the performance is done in a way that is assessed as business entity achieves the objectives in terms of procurement, production, sales and the like. From the above stated may be concluded that the primary purpose of auditing is the assessment of performance in the operation of the business entity and identifying areas where it is possible to take measures to improve the operation of business entities. Unlike previous revisions, in this review there are no predetermined standards, so the dilemma is how the auditors in advance to determine the standards, rules or regulations to perform the evaluation of efficiency and effectiveness. It follows that auditors must choose measurable criteria that are always found in the area of many principles of economics and organization of the operations

of economic entities. Against this background it can be concluded that a review of the operation has the following features as:

- Auditors who conduct audits are independent of the activities we reviewed (eg. Auditor may be employed in commercial service or its head, and is also audited the commercial operations of the business entity);
- The auditor is employed in the business entity in which the audit;
- The auditor submits the audit report and submit it to officials in the business entity. It shall mainly refer to the identification of problems related to effectiveness and efficiency in business operation entity.

### **3.2.Judicial review**

Judicial review is intended to detect or promotes activities which consequently have fraud or other illegal activities, integrated in the financial statements of the business entity of the audit client. With the growing number of business entities and their financial reports, despite legal and other measures, increasing the number of fraud and judicial review has obvious growth. Judicial review, usually are conducted in the following cases:

- Business fraud made by internal and external stakeholders of the business entities;
- Criminal investigations;
- Confrontations and disputes between partners, shareholders and managers;
- Economic losses, and
- Civil disputes

### **3.3.External Audit**

One of definitions for external audit shall be defined as subject to the accumulation and evaluation of evidence about information for determining and reporting system between the data and established criteria. From this definition we can conclude that the notion of external audit is broader audit of financial statements and includes numerous services to ensure the quality of the information presented above for the owner of the business decisions. Regardless of the treatment of external audit is an undisputed fact that its implementation is conditional on the existence of the information presented in verified form and certain standard criteria based on which the auditor will evaluate. The audit should be conducted externally complete and professional person in his work will absolute independence from the management of the client. Regardless of the trends to expand the scope of audit services offered to clients, external audit is commonly equated with the audit of financial statements. External audit to provide protection to the interests of capital owners and at the same time to offer reliable information to other users of audit services, such as shareholders, creditors, potential investors, employees and the general public. If we consider the complexity and the activities to be implemented external revizors for the successful functioning of this review is related to quality regulations, audit standards and code of professional ethics.

### **4.Internal Audit**

Unlike external, internal audit occurred as a result of the needs of modern businesses to introduce their own, internal and additional form of supervision in order to perform such control examination system of internal controls performed by all employees as part of their

duties, to evaluate its effectiveness, discover weak points in its operation and propose measures to eliminate the appearance of weakness. In other words, the internal audit activity is organized by the management of the business entity or other business entities to assist in the evaluation of the operation as a whole or to individual segments. In terms of business and management functions in enterprises, internal audit can be monitored as part of steering control, where business functions are subject to examination in order to perform more efficiently, thus ensuring the functioning of an information subsystem which however, the guide provides information for making appropriate business decisions. According to the definition of the Committee of audit practice (Auditing Practice Committee-APC) Internal audit is an element of internal control system set by management of the business entity, banks or other institutions for examination, evaluation and reporting function of accounting and other controls in operation. Internal audit is introduced in order to improve the decisions of managers or to satisfy statutory requirements. Institute of Internal Audit in the UK, apart from this definition, the internal template defines as an independent activity in the corporate assessment of the operation, established as a service office of the corporation. It is a control function that works by evaluating the adequacy and effectiveness of other controls and supervision. From these definitions can freely conclude that the primary task of Internal Audit, through sight and evaluation to assess the activities of the business entity, to provide adequate assistance to owners and management of the business entity in order to more effectively engage them to perform undertaken professional activities. For this goal to be achieved, the internal audit of users of this type of service offers numerous analyzes, suggestions, recommendations, advice and information directly related to activities subject to internal audit.