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The Civil And Legal And Criminal Liabilities Of Auditor

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Abstract: This study shows the importance of internal regulation of the auditor to the clients and beneficiaries from auditing services, and shows how audit service need to be highly professional and accurate and satisfy client's expectations. The study also identifies the role of auditor and his/her legal and criminal liability due to detected fraud or material misstatements as well as illegal acts found in the financial statements. In addition to that the study emphasizes on the contracting responsibility of the auditor towards clients and others, and shows auditor's role and positions that not derived from previous lawsuits but from the current laws and regulations issued by legislative bodies the of the country. The study found that the liability of the auditor about the audit reportis the same whether the illegal acts produce direct and important impact or less important and indirect effect. It is auditor responsibility to inform the audit committee or any other groups that have authority to control and take actions in case of illegal acts that was detected by the auditor.

Key words: Auditor's internal regulation, civil liability, legal liability, criminal liability, fraud and misstatement, gross negligence, accidental negligence, contracting liability, clean opinion, unqualified opinion, material misstatement, illegal acts

INTRODUCTION

The Legal liabilitiesof auditor in detectingmaterial misstatements and frauds in the financial statements and illegalacts put the auditor it in front of criminal and legalliability and important responsibility to inform the specialist authorities about any kind of fraud and material misstatement. Due to the important role of financial auditor in detecting illegalacts that would be discussed later in this study, therefore there are a number of regulations that organize auditor's work and task as well as specifyingauditor's responsibility and duties by the authorities of the auditing in particular in United States and UK, as these two countries are considered a good example of famous regulatory bodies that are committed to common audit and internal audit, also because most of the countries in the world affected by the auditing bodies of these two countries.

Internal Audit Regulation And Expectations:

The auditor must do the job in quality and in professional way as expected from the clients so that to contribute in economic development. Professionals always specify the suitable levels for auditing work quality by putting recognized auditing criteria and certification standards and rules of professional behavior. Despite these standards and regulation determine the service quality provided by the auditor but it obliges to grant a special mechanism to monitor the occupational performance, and this is an important matter to sustain the desired service quality. If the auditor takes the responsibility on contrary of the standard behavior then there should provide special ways to limit such contraries if happened and specify punishment disciplinary and legal actions to be taken about it. The occupational organizations play an important role in controlling the quality of occupational services with interferesby the judiciary system if these efforts of these organizations failed. (Hendrickson, H. 2001)

The implementation of executing the ethics standards through the occupational organizations is called "self regulation", but the monitoring and correction procedures that followed by the government authorities and judiciary system is called "external regulation", and for the internal regulation to prevail from the auditing services then beneficiary should obtain these services at the desired quality level identical to their expectations, and the differences between the understanding of beneficiary and auditor to service quality, and in particular to what is associated with the certificate occupation, and called "gap of Expectation", and this is the difference between what is expected from the beneficiaries from financial statements of the auditors and between what the auditors believe they can do.

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It is important areas that contribute to the existence of this gap include: (Cousins, J., Mitchell, A. and Sikka, P. 1999)

1. The responsibility of auditor for detecting material misstatements and frauds: Many clients who are usingthe financial statements that the express of auditor to something clean means that auditor already has discovered all significant errors and cases of fraud that may have occurred during the period under auditing.

2. The accepted standards of auditing do not comply with this belief, because the auditor according to these standards is responsible only to practice occupational care that should be fulfilled when making the auditing procedure. If the management deliberately has skipped the control procedures or commit other types of fraud woven in collusion with staff and competently managed to hide them, then doing the imposed occupational diligence may lead to detect the distortion of the financial statements resulting from these methods.

3. The auditor responsibility associated with the ability of the projects ofauditing client to continue to engage in the activity: most users of financial statements believe that when the auditor expressesa clean opinionthen it would be a testament to the strength of the financial position of the company or the bank and its ability to continue to engage in the activity. If the company goes bankrupt later or exposed to the financial difficulties, then the users of financial statements are wondering: Why the auditor did not discover these things from the beginning and indicated them in the audit report.

4. The auditor finds that users do not distinguish cleanly between the failure of business projects and audit failures. The failure of projects occurs due to mismanagement or strong competition or unfavorable economic conditions or a combination of all the mentioned above. While the audit failures occur because of a lack of commitment by the auditor to the generally accepted auditing standards.

To clarify what is mentioned above, if the auditor showed a clean opinion in the financial statements of a particular company or bank or any economic entity, and the time of stating the opinion, all available evidencesprovided for the auditor shows that ability of the company to continue in doing the activity, and after short period some sort of unexpected events happened, such as a sharp decline in the level of economic activity or competition intensifies so that the company could not face the consequent inability and to continue in its business and then go towards bankruptcy, and this is an example of business failure. If we assume that there was available evidence for the auditor at the time to express an opinion, the company shows inability to continue in doing business activities, and because of neglect and indifference the auditor did not check the available evidences and then issuing a clean opinion about them, this is called a "Failure of Review".

The occupational authority in the United States have realized the existence of this gap and its seriousness, so it worked to overcome this gap by issuing new auditing standards associated with the material misstatements, frauds, and assessment of auditing ability to handle the clients projects to continue in doing business and encourage the companies to establish auditing committees belong to the board of directors to supervise the process of financial reporting and judging the differences between the auditor and management. The occupational authority obliged the auditors to continuously acquire the occupational education, and to know the latest auditing and training science, and possess the necessary skills of auditing. (Sprague. William. D., 1988).

The Legal Liability Of Auditor:

With regard to auditing of financial statements, the auditor may be accusedof accidental negligence, or gross negligence orconstructive fraud, and in cases of negligence, the defendant must prove it by the following:

1. Financial Statements include substantial distortions (errors or fraud).
2. The defendant relied on financial statements and the defendant has been damaged as a result of this dependence
3. Applyingthe generally accepted auditing standards should lead to the discovery of these distortions.

In the following section we will illustrate thebetween ordinary negligence, and gross negligence and Constructive fraud.

Accidental Negligence:

Accidental negligence means that the auditor do not make professional care and complete implementation of the audit procedure and due diligence means the use of knowledge, skill and exercise personal judgment available to practitioners in similar practice conditions. Accidental negligence is unintentional or a simple lack of interest without any attempt to deceive or a deliberate any kind of intention to cheat. For example, due to the lack of notice and careless, the auditor could not identify an important commitments or obligations in the financial statements.

Accordingly, in the case of accidentalnegligence, the allegation is that the auditor did not do his jobwith high interest and professional care that expected from him/herasaccidental auditor in similar cases, and then the auditor could not detect errors or constructive fraudsthat could possibly be discovered if the auditor was committed to the auditing standards, which will be explained in next sections

Gross Negligence:

Gross negligence representsstrong and flagrant violations to the standards of due diligence and efficiency in the performance of occupational duties. It means that the auditor failed to do the minimum care expected to be done by the auditor in similar cases, and the consequent of gross negligence is lack of ability to detect series and highly important material misstatements or frauds instancesthat should have been detected through applying the general auditing standards

It is important to distinguish between two types of negligence because the auditor always asks for gross negligence, but should not permanently be responsible for ordinary negligence. There are two main concepts that help to distinguish between the auditor's responsibility for ordinary negligence and responsibility for gross negligence, which are the relative importance and internal control or internal audit.

The Relative Importance Of Distortion Or Material Misstatements:

As the relative importance of distortion (frauds &material misstatements) increases, then the probability of detecting such distortions by the auditors increases as well. If the client did register fake sales with high values at the end of the year in order to increase profit of sales, then applying the accidental or regular procedures of auditing alert the auditor to the existence of these fake sales

If the auditor failed to detect the intentional distortion, then this kind of negligence will be interpreted at a gross negligence when legal actions taken against the auditor. There are many expenses and accountings, and some of them were reduced to small values so that each of these distortions is not important in particular but there impact on the community is vital and may lead to significant distortion to the actual profits, and may be equal to the value of fake sales as in the previous example, however in such case, so therefore it is not possible that applying usual regular auditing (Stereotypy) will lead to detection these small value distortions, and accordingly the possibly to be detected by the auditor is very weak. If such case has happened then the failure to detect the distortion will be interpreted as Ordinary negligence and not gross negligence, even though its impact on the income is big and significant.

The Internal Control In The Accounting Process:

It is part of internal control that is designed to increase confidence in the accounting records and assets protection. According to auditing standards; auditor should determine significant weaknesses in accounting controls and then expands in the verification choices in those areas. It is possible to expect that the auditor detects important financial statement distortions in that occur because of major weaknesses in control (within the system). However, the distortions resulting from fraud may occur through collusion between some employees to avoid the get around the auditing system or by avoiding that by the management or ignoring internal audit, such kind of distortions are extremely difficult to detectby the auditor, especially with the existence of sophisticated and smartways to hide the facts. For this reason, the allegations concerning negligence claim would be very difficult to prove in these circumstances.

In one of the cases submitted to the US court (Cenco&Seidman, 1982) the auditor was judged not guilty, because the auditor failed to discover the a fraud in the storage equal to 25 million US dollars that that management was able to hide. The judge stated in his decisionthat the auditor was not able to verify or discover such kind of fraud when the management transferred the company to a place of burglary by collusion with external parties. This case is a good example of ignorance by the management to conduct internal auditing and occurring of fraud outside the internal audit system.

This means that fraud and critical errors that occur because of the presence of vulnerabilities substantial in the control system is very likely to be discovered during the auditing procedure compared to those resulting from causes outside the control system, because auditor expands theverification and test processes and balances under the conditions of weak internal control system. Accordingly, it is as a general case, it can be assumed that favor for the discovery of the distortions that occur within the control system is more indicative of gross negligence in failing to detect distortions that occur outside the control system.(Issa, Abdul Wahab, et al., 2005).

Fraud:

Fraud is the existence of deliberated intention to deceive others or intentional distortion to financial statement, and if the auditor shows a clean opinion about financial statement and provides misleading information, even knowing the facts, then the auditor will be accused of fraud because of intentional deceiving and distortion of others, accordingly the auditor must be prosecuted because of fraud after providing the following conditions:

1. The auditor showing the fake facts
2. The intention by the auditor to deceive others
3. The intention by the auditor to make others relying on false presentation of facts
4. Justifiable reliance by others on the false presentation of facts
5. Covering the losses by others because of this dependence

For example if the auditor has a clean opinion about financial statements and knowing the net profit is highly inflated (false offer), and the auditor submit these statement to the client after being reviewed and giving a clean opinion about them and auditor knows that the client will submit these statements to financial institute that may approve loans for the client (the intention to deceive and the intention to convince the financial institute to rely on these statements) and therefore the financial institute permitted to give the loan to the client based on clean opinion of the auditor and his/her report (justified reliance), and after discovering the inflation in the net profit, the client announce bankruptcy and do not pay back the loan to the financial institute (losses due to reliance). In this case the financial institute could sue the auditor and win the lawsuit based on fraud allegation.

It should be noted that negligence does not involve deception, the auditor may have failed to do his job perfectly, but did not intentionally deceived a third party by cooperation with the client using the financial statement to make specific decisions, however the negligence may be very big and approaching or similar to deception., and if the auditor ignored a clear evidence or the auditor has no evidences to approve that the financial statements fair and though expressed clean opinion, then negligence in this case are of such magnitude that leads to draw a kind of fraud and deception called "fraud juridical",i.e it is a deception even if it does not prove the existence of a deliberate intention to deceive others.

The Legal Liability Of Auditor Towards Clients:

The common law relies on several legal resolutions issued by the courts in previous cases, may belong to old decades, and the common law does not require the auditor to prove or guarantee that the auditor is impeccable, but the law requires high accuracy when doing the auditing with high skill and professional auditing job. The defendant will try using common law to prove that the auditor does not practice the required consideration because the auditor disagrees with the generally accepted auditing standards. According to the common law the auditor should be liable towards his/her client on violation of their contract. The auditor may be responsible towards third party as well.

The Contracting Liability Of Auditortowards Clients:

The client is defined the person who has signed a contract with the auditor, or the authorized person on behave of the client, or the person who do reckoning of accounts in case of bankruptcy, or working in any other state that enable him to claim against the auditor completely as the client himself. The base of this responsibility is the contracting relationship between the client and auditor that specified by the singed contract between them in particular in personal deals and personal companies when the auditing is optional. According to that the contract the auditor should do his work at high accuracy and professional skill with accordance to occupational principles. However if the auditor neglect doing his professional duties, then he/she will be responsible for compensating the damage done to the client As a result of the gross negligence and fraud.This contractual responsibility towards the customer called in the common law, "the privacy of the contract."

The Liability Of Auditor Towards The Others:

The meaning of others or third party is all parties (regardless the client who signed the contract with the auditor) that depends on financial statements and financial accounting information required for various economical decision making such as current & future investors, and the creditors, banks, and government, and personnel…etc

According to the common law there is no contractual relationship between the auditor and the third party and therefore the auditor is not liable towards third party for accidental negligence but the auditor will be liable for compensating third parties for the right of the damage as a result of gross negligence or fraud, and the burden of proof in this case on the third party, who must prove the existence of substantially distorted financial statements , and there are reliance on these statements , and there is damage caused by this reliance.

We have previously referred to the clients of auditor have a common law relationship called "the privacy of the contract," which is a contractual relationship between the auditor and the client for the performance of professional services. The clients are the only persons who can rely on this privacy relationship to successfully prosecute auditor for accidental negligence, according to the common law.

This relationship does not extend to non-clients because the auditorshave no control over the identity or the number of non-clients who rely on audit report or on the importance and value of risk that may be exposed to non-clients as a result of reliance on the audit report. Hence, if privacy relationship is extended to the third party, then the liability of auditor may not be equal to the amount of audit fees and the value of fault or negligence which has committed by the auditor. (Farje A.,1993)

But in some cases it may be auditor’s responsibility to third parties for accidentalnegligence, like the client, and these cases are “Primary Beneficiary Relationships” defined as a relationship which identify the client to the auditor as an appointed auditor specifically to do the review for the benefit of a specific third party and the objective of the auditingis to make this party depending on its results to make a particular decision, so the third party was able to prove the primary beneficiary relationship with the auditor, then the third party will have the right to sue auditor just like client for accidentalnegligence in accordance with the provisions of common law when two conditions available: the first condition is that the third party is known specifically to the auditor, and the second condition that this party is the one who will get the basic benefit of the auditing process.

To explain that, for example; the expected buyer to the company request from the owner to appoint auditor to witness and verify to the accuracy of the financial statements as a condition of purchase, and that the expected buyer is known by the auditor, and it has been said to the auditor that this auditing process will be for the benefit of the buyer to take the decision to buy the company. In this case, although there is no contractual relationship between the expected buyer and auditor but there is a main beneficiary relationship and then liability is on the auditor torespect responsibility towards the expected buyer in the same level just like toward the client.

Foreseen Known Party Relationships:

The other (third party) may has the right to sue the auditor because of accidental negligence according to the common law if the court saw that it is a known party or expected to be known to the auditor and the third party will consider the work of auditor to make specific economical decisions and the relationship of the known party is more distant from the main beneficiary because the known party is not confirmed to the auditor as a main beneficiary, but the third party is a person or a group of persons known or may be known to the auditor as considering the financial statements that should be reviewed. There are two indicators that could be relied on in order to specify the known parties, which are:

- Knowledge of the party to a particular person or group of persons
- Knowledge of auditor on specific financial process or identical financial processes

For example; if the auditor accepted an offer to review the financial statements of a company, and he/she knows that the company is negotiating with the bank to get a loan and that the financial statements have been audited will be provided for this particular bank for use in the assessment of the granting of the loan. Accordingly, the knowledge of auditor to specific persons (the Bank) and knowledge of specific financial process (expected loan from the bank for the company) is giving the bank the relationship of known party with the auditor.

On the other hand, if the auditor knows that the company is negotiating with one of the many banks that deal with them in order to get a bank loan, and that the financial statements that have been audited will be used to grant a loan with one of these banks. However the knowing of auditor on specific groups of people (group of banks that deal with the company usually) and knowledge about certain financial process that might give any of these banks relationship with known party by the auditor, although the auditor did not know the bank, which may grant the loan and on the time of signing the agreement on doing the auditing.

Foreseeablepredicted Party Relationships:

The expected parties are parties with farther distant with the auditor from previous relationships, and they are representing the users of financial statements that have been audited and are not known precisely for auditor, or they are who used the financial statements for the purpose of unknown financial transactions precisely known by the auditor, but they are reasonably expected to reviewfinancial statements and act or cease from acting because of reliance on them.

In some countries, especially in the United States, the courts allow the expected parties to sue the auditor for accidentalnegligence according to the common law, and no doubt that this opens the door for the prosecuting the auditor by a big number of financial statements' users that have been audited, although the auditor did not know specific transactions which may be used for which those financial statements. And because of wide responsibility,the negligence criteria usually do not apply to the expected parties.

The Liability Of Auditor In Accordance With The Existing Legislations:

This liability is not derived from the jurisprudence of the courts, but from the applicable laws in the state and issued by the legislative authorities. The prosecutor can use the existing legislation rather to add to the common law in cases where possibly apply such legislations.

Some of these legislations imposed performance standards on auditor more stringent comparing to the common law. In the United States, for example, it is in conformity with the securities law issued in 1933, the prosecutor can sue the auditor successfully for accidental negligence whether the financial statements contain material misstatements or omittedmaterial, and the prosecutor could approve the loss.

It is not the responsibility of the prosecution to prove negligence by the side of the auditor (but the auditor should prove that he/she was not negligent), or proof of reliance on the audit opinion or a causal relationship between the misrepresentation or omission and the loss borne by the prosecutor, or prove the existence of a contractual relationship between the prosecutor and the auditor.

It is obvious from the mentioned above that the prosecutor will use the current legislation to prosecute the auditor if the circumstances of the case permit to do that.(Issa, Abdul Wahab,2005)

The Criminal Liability Of The Auditor:

We have explained above that civil liability of auditor to his client and to the third party which gives the right to who have borne loss from the actions of auditorin order to obtain compensation commensurate with the injury of damage. From the perspective of the criminal liability, the damage goes beyond the scope of the party who relied on accounting information to the community as a whole. The auditor could be considered a criminally responsible person if the injury of damage does not affect a single person but affects society as a whole.

The Egyptian Companies Act No. 159 of 1981 acts has specified the actions that require asking the auditor criminally including: proof of false statements in a news release stocks and bonds, or the ratification of the dividend or interest otherwise the provisions of this law or the company, or intentionally put false report on the outcome of the review, or concealment or omission deliberate the facts essential to the report, which provides the General Assembly, or fraud in the company's records or proof incorrect facts or prepare reports containing false statements the will be used to influence the Assembly resolution, or assisting and agreement with any financier or facility on the tax evasion stipulated in tax law in whole or in part.

The criminal liability is a personal liability, any person did actions against the law, should bear the penalty such as fines or prison or both of them.

The Role Of Auditor In Avoiding Legal Liability:

No doubt that the auditor will attempt to prevent any legal prosecutions against him/her or defend himself/herself in case of suing him/her.The best way to prevent taking legal actions against the auditor is to terminate the bases that construct these procedures:

1. Allocating large amount of auditing efforts for cases of high risks in order to detect material misstatements and fraud cases
2. Verifying that the client has made correction to major misstatements that was detected in order to prevent harm and injury to the third party due to reliance on financial statements with material misstatements
3. Taking aid of auditing committee related to board of directors as possible. This Committee is composed of members of the board of directors and is responsible for monitoring on many things including internal monitoring system and judge on problems that arise between the auditor and management.
4. Supervising with care on the assistances and checking their works
5. Failure to comply with time pressures during the auditing, therefore the client may push to finish the auditing earlier comparing to what is required in current conditions, and even though finishing the auditing earlier may reduce the costs on the client but it may stop the auditor to detect important material misstatements in the financial statements because of non-completion to the necessary auditing procedures.
6. According to the new auditing processes, it should call the previous auditor and being careful before accepting a new auditing job in order to avoid doing auditing to financial statements belong to companies having dishonest management, and because such connection is contrary to the rules of professional job and increases the likelihood of errors and significant cases of fraud that can't be detected in the financial statements, in addition to that the current clients must be assessed every year according to the same reasons mentioned above
7. Taking care of professional conduct and spending active efforts to serve the interests of the third party, and preserving the objectivity and keep honesty, also freedom from conflict of interest as well as avoiding distortion of facts, and avoiding to subdue auditing review to others

But regardless of how diligence occupational due, the auditor will not be absolutely sure that all the material misstatements and significant cases of fraud have been discovered and corrected properly reflected in the financial statements. Auditing is based on optional basis and then there is a risk of material misstatements, fraud and were not detected. For this reason the active and smart auditor may be prosecuted by the third party who suffered from damage depending on financial statements with material misstatements completely. Therefore the auditor should prepare to defend himself/herself in case of legal action against him/her by the client or a third party, and the best defense is to prove the practice of professional care due in the auditing process, and the best proof of this is documentation to the whole auditing process and the most important worksheets that help in providing carefulness as follows: (Brenda Porter, et al., 1998)

1- Documentation of vulnerabilities that were discovered in the internal control, and how testing and verification programs was modified in the existence of these vulnerabilities

2- Documentation of auditing estimation of fraud and the actions taken in the light of these estimations.

3- A letter of confirmation to do the auditing task that clearly specific the nature of services that should be fulfilled by the auditor

4- Evidences the work of assistances was fully verified and all non-answered questions was declared before issuing the audit report.

The Liability Of Auditor In Fraud And Illegal Material Misstatement:

Any financial statements processed by the auditor may contain incorrect elements that produce misstatements or frauds or illegal behaviors. The auditor bear some responsibilities to detect such matters and reporting about them, and according to that misstatements will be discussed and the way they happened and the responsibility of auditor to detect them and reporting about them, then discussing illegal behaviors and auditor's liability.

Material Misstatements And Fraud In The Financial Statements:

Definition of Misstatement: It is unintentional errors. Material misstatements relates to the information included in the financial statements.It is divided into deletionmisstatement (ie, excluding operations or assets of the financial statements), and commit errors (such as the inclusion of financial statements on false balances or processes). When examining the auditor's deletion misstatement, the auditorbe interested to confirm the completion, while the errors of commitment are associated with confirming the existence or occurrence, therefore misstatement may result from:

1. Non-registration of some operations, such as non-registration of some suppliers' bills near the end of the year, which leads to the show purchases and suppliers undervalued.
2. Recording misstatement values, such as non-registration the correct values of sales invoices that may lead to incorrect deportation values of accounts receivable and sales, and record some of the processes in improper accounting period.
3. Disregarding some facts or misinterpretation which causing improper accounting estimates, for example: The credit manager maybe very optimistic in the assessment of expected collections from debtors with significant balances, this situationlead tovery low custom estimate for doubtful debts.
4. Poorimplementation of accounting principles relating to evaluation or rating, view, or disclosure of accounting. For example, consideringthe expenses to maintain machines, mistakenly, as additions to the machines, resulting in amplification in net income and the value of machines, or ignore the fact that credit balances in accounts receivable should be classified as short-term liabilities, resulting to show all of the current assets and short-term liabilities undervalued.

It is obvious from the above that the misstatements lead to a distortion of the financial statements but are not reliance and unintended, and if were detected, then personnel become united to correct them, these misstatements can be reduced by having an effective internal control system.

Definition Of Fraud:

fraud is more serious than misstatements because unintended result of deliberate distortions and include Embezzlement and misleading financial reporting. The embezzlement is the transfer of assets using fraud and deception from the company to one or more of dishonest employees. In other words embezzlement is the act of dishonestly withholding assets for the purpose of conversion (theft) of such assets by one or more individuals to whom such assets have been entrusted, to be held and/or used for other purpose. This transfer maybe proceeds by some form of hiding the truth. For example, a dishonest employee embezzle the collected amount from a debtors and avoid recording the amount in the record books and trying to hide the embezzlement by deducting the amount from debtor's account and making the suspected allocateddebits owed him.

The misleading reporting process consists of several attempts by management to distort financial statements in order to mislead and deceive users of those statements. The Auditing Standards Board of the American compound of Chartered Accountants has explained that the following actions involving or describes a process of preparing misleading financial reports:

1. Forging, altering or tampering in the accounting records or supporting documents, which are used to prepare the financial statements them. For example; issuing sales invoices of fake sales, resulting in accounts receivables and inflation and deliberate inflation in the value of sales.
2. Misrepresentation or omission for approved events or financial transactions or other important information in the financial statements. For example, non-disclosure of the financial statements of the unit for outstanding issue is likely to be the result of separation which is opposite the benefit of economic union or bank.
3. Poor implementation adopted in doing accounting principles values, or classification or through presentation, or disclosure. For example, the client buys another project which was accounted for in a way ofinterests merger rather than the method of buying, even though all the evidence supports the classification process as buying process.

.Sometimes it is easy to differentiate between misstatements and fraud, in other cases separation can be difficult, for example, if sales invoices included (mistakes) unintended calculation they are considered mistakes, while the action of making sales invoices for fake debtors is considered a fraud. On the other hand, the reduction approved for doubtful debts may result from misinterpretation is not relied to the ability of debtors to repay or deliberate attempts to increase net income and on this basis, the auditor's liability for detecting material misstatements and fraud in the financial statements are the same.(Michael c. Knapp.,1991).

The Liability Of Auditor In Detection Of Material Misstatements And Fraud:

The auditing standards specify the auditor in this field as follow:

1. The auditor must estimate the possibility of risk of making faults or fraud in the financial statements that contain major distortions
2. Depending on this estimation the auditor must design and execute auditing so that to provide a reasonable degree of certainty that misstatements and major fraud instances could be detected in the financial statements
3. Since the opinion of the auditor about the financial statements relied on reasonable certainty then the auditor is not certain or guarantee and auditor’s report is not representing an absolute guarantee.
4. According to that, if later misstatements have been discovered in the financial statements then this is not considered evidence on insufficient planning or executing auditing or defect of personal judgment from the perspective of auditor.

There are several warning signs that could indicate the presence of fraud and, such as:

Weaknesses in the internal control system, or ignore management control procedures and the presence of large losses in the stock, management ignorance to the results of both internal and external audit and the presence of accidental operations with the bank, and a significant increase significantly in expenses and purchases. There is no doubt that the existence of such things could urges auditor to consider specific areas of review as high-risk areas and take appropriate actions accordingly, such as the allocation of qualified auditors for review the financial statements, and implement audit procedures that enhance accidentalaccounting procedures that are affected by these processes.

Audit Planning To Detect Fraud And Important Material Misstatements:

At the level of the financial statements, the auditor should take into consideration a number of things when making a decision on work’s requirements to provide a reasonable degree of certainty that help to detect fraud and important faults and misstatements, and these issues are:

There are administrative properties which are considered as clear signs of the existence of fraud risk and misstatements such as: control of one person in management, the existence of the hostile attitudefrom the management toward financial reporting, high rate of turnoverin management positions and members, unusual focuson achieving high and unexpected profits, and bad reputation of the management department in the business community. In such circumstances the auditor should determine the feasibility of continuing to work with the client or not. If the auditor decided to continue then he/she must exceed the scope of audit to verify the increased risks resulting from these factors..

Some operating characteristics and industry characteristics may show signs of the existence of fraud and misstatements. Client may be less profitable than other companies in the same industry, profits may be volatile substantially with general economic conditions. The industry itself may be in decline, or the company may have central disinfected operating procedures. These operational characteristics may lead to an increased risk of misstatements or fraud because of the desire to show effective performance. The auditor should when doing planning the audit procedure to takes into consideration the expansion of audit procedures to hedge the growing risk from potential distortion to financial statements

Specific characteristicsinauditing task may show the auditorrisk signals. If the auditor has to deal with many of the complex accounting issues, or difficulties in reviewing some of the stocks and the financial operations of the client, or finding many faults and misstatements fromprevious audit. It is necessary therefore the auditor should plan to expand the audit procedures undersuch circumstances.

At the accounting level, the auditor must take into account many things when deciding the scope of the audit, including the following:

1. The accounting matters affecting a particular account balance may be complex or *controversial*.(Arabic Academic Dictionary)client's business is salesof clothing, according to the latest fashion lines, which are very well known during limited periods of time. In this case, the estimate value of increment in stock will depend largely on thepersonal judgment, which could create a contradiction of views between the auditor and the client which requires additional review effort to calculate the stock.
2. The detection ofimportant distortions in account balances in previous audits precedent, for example, if the client was usually trying to show balances creditors undervalued by deleting purchase invoices with big cash values, then the auditor must have a plan to spend more timein such cases in order to examine the accounts of creditors because of the potential risk arising from possible occurrence of same distortion in the current year.
3. Determining the balance of the account may require a great deal of personal judgment bythe client of the auditor. For example, if the client sells goods depending on guarantee contracts that produce many

unpredicted claims or estimated claims, which includes mainly depend on personal judgment, such case requires a comprehensive reviewsand fast actions.

The Liability Of Auditor To Detect Material Misstatements And Fraud:

What the auditor should do if thevalues found in the client's accounting records are different from the values that have been audited? It is necessary that the auditor decide whether these differences as a result of unintentional error or fraud in particular. Faults and misstatements require correctionthe records of client's accounting, the fraud it more serious implications, extends beyond the monetary impact on the financial statements.

If the auditor determines that this difference is due cheating or fraud, but its impact on the financial statements may not be so important, then the auditor should do the following:

1. Refer this matter to the appropriate administrative level, at least to a highermanagement position from the position that involved in the fraud
2. To convince himself that the impact of fraud on other sides auditing has taken the appropriate attention.

For example,if the auditor discovered that the Secretary of expenses fund has withdrawnunauthorized amounts from the fund, this action must be reported it to the supervisor of the fund or a higher level and must be treated immediately as fraud action. This embezzlement may have acted individually isolated from an employee in the low level of job position, and then there would be no need to track more actions like that. If other duties from this employee has other tasks to do such as preparing portfolios deposit to all collection of sales, then the auditor must report the fraud to appropriate administrative level, and to take into account the possibility of embezzlement of some cash receipts from sales in the future.

As if the auditor determines that this difference, or may be, fraud and its impact on the financial statements may be important, it should References:

1. To determine the impact of such fraud on other aspects of auditing procedure.
2. To discuss the matter with the highest management level rather that theorganizational level involved in the fraud action.
3. Trying to get accurate evidence to prove the fraud action and its potential importance on the financial statements.
4. To propose to the client, if possible, to consult a legal advisor or consultant in similar cases.

For example, if the auditor discovered that teller skims the daily cash receipts, this is more serious than stealing from the cash fund because it significantlyaffectthe accounting of many financial statements.

The auditor should expand in the audit procedures for many of the accounts that were affected by such embezzlement (cash, debits, etc.). In addition to that there should be a discussions with higher administrative levels from any employee involved in fraud and advise the client through consultation with legal advisor.

The Impact Of Fraud On The Auditor's Report:

The responsibility of the auditor extends beyond fraud to the opinion shown in the audit report, the financial statements must be modified if necessary or making a qualified opinion or adverse (negative) opinion if required in the financial statement report.

Sometimes the auditor may not be allowed, or you may not be able to, implement the necessary audit procedures to conclude whether probable fraud could affect the financial statements or not. In such cases the auditor should do the following:

1. To avoid giving opinion on the financial statements or express an unqualified opinion.
2. To report the results on potential fraud to the Audit Committee of the Board of Directors

Because of the circumstances described above, the auditor must quit from the audit process.

Illegal Acts:

Illegal acts represent the violations of the laws or government regulations by the department under audit, management or employees who work for it.

It is not included in the context of this definition, whether the personal behavior committed by the personnel employed byclient was out of client'sactivity, and even the auditor in a position that enable him/her to detect possible illegal acts such as some employees get lower than standard salaries. But the final decision regarding illegal acts should be decided by a specialist person in law. The responsibility of the auditor against illegal actions is subjected to detect illegal acts and making reports about them.

The Liability Of Auditor In Detection Of Illegal Actions:

Some laws and regulations have a significant and direct impact on the values found in the financial statements, for example, tax laws affecting expenses. The liability of auditorin detection of such behaviors similar to liability in the case of fraud and misstatements is that: the auditor should estimate the risk of illegal actions that affect directly the values of financial statements, and depending on this estimationthe auditor should design and plan audit procedure to a reasonable degree that guarantee the detection of illegal acts.

On the other hand there are other laws and regulations have a significant impact, but not directly on the values found in the financial statements, such as laws and regulations on job security and protection of the business environment. And usually cause indirect impact on the need for the disclosure of contingent liabilities due to expected losses as a result of fines and possible sanctions because of expected losses as a result of fines and penalties, and suspension of operations.

The auditor may not know the existence of such illegal actions unless the client telling the auditor or perhaps in other ways, however it is the liability of the auditor to discover these types of illegal actions, in addition to that the auditor should be cautious of probable illegal actions, and if the auditor knows specific information that provides evidence concerning the existence of possible illegal action which may have a significant impact indirectly on the financial statements, in that case the auditor should applya special audit procedures designed to verify the extent of illegal actions.

The Liability Of Auditor In Reporting Illegal Actions:

The liability of auditor about the report is the same whether unlawful conduct with a significant impact and directly or with significant impact and indirectly, where the auditor must tell the audit committee or any other groups has a particular the authority and responsibility to act against similar illegal actions. This contact should describe the behavior, and the circumstances that lead tothe occurrence of such illegal actions, and its impact on the financial statements. This contact may be orally or in writing, and if orally the auditor should document this contact.

If they are punishment for illegal actions or appropriately disclosingthe information in the financial statements, the auditor must give a qualified opinion or an adverse. If the client has prevented the auditor to collect sufficient evidence in order to properly identify the extent of illegal actions, then the auditor must refrain from giving any opinion because of the restrictions imposed on the scope of the audit procedure.

If the client refuses to accept the amended report (qualified opinion or omission to express an opinion), the auditor should take into account the possibility of withdrawing from the audit process and to provide the reasons for this withdrawal in writing to the Audit Committee of the Board of Directors. (Obaid, Yahya Hussein, et al.,2001)

Conclusion:

This study discussed the main issues and aspect of audit procedures and auditor criminal and legal liabilities during the auditing process, and whether the auditing procedures are financial and well audited according to the international auditing and occupational standards. The study showed that the auditor needs to be highly responsible and spend the best efforts to verify the financial statements before submitting the report to the client or beneficiary from the audit report. The study found that the legal nature of audit's work through verification of the correct allegations of the client and the values indicated in the financial statements, and commitment to follow the accounting principles in processing all accounts of the client. The study emphasized on the high importance to prepare a summary of all audit works in auditor's report.

The responsibility facing the auditor in case of commitment to violation of occupational law is determined by the type of committed violation, as well as stating by the laws and regulations of each country differently, where the main liability of auditor in breaching the conditions set forth and issued by the Accounting and Auditing local and international bodies alone between the auditor and the company, and whether theses misstatements and faults were gross or accidental.

This study focused on the legal, criminal and civil liability of the auditor with regard to the self organizing and expectations to accidental and gross negligence, and the relative importance of distortion or misstatements, in addition to that the concept of internal monitoring in the accounting process and fraud, and the legal and contracting liability of auditor towards the clients and others, then the criminal liability of auditor was mentioned and discussed the role of auditor and his/her position from the legal consequences of fraud and illegal misstatements in the financial statements, and the impact of fraud on auditor's report and illegal actions of the auditor, adding to that the main responsibility on auditor's role to detect any illegal actions and fraud.

Recommendations:

1. The auditor must plan for the auditing procedures using doubtful assumption, in particular matters that may bear potential risk because of materials distortion in the financial statements resulting from fraud and illegal acts
2. The auditor should understand the probability of distortion in financial statements due to fraud and illegal acts, in addition to that understanding the accounting system and internal monitoring applied in preventing faults and misstatements

3. When the auditor facing conditions that refer to the existence of material distortion in the financial statements resulting from fraud or misstatement, then the auditor should execute the procedures that verify the distortion in materials. The modification depends on the nature and timing and the extent of essential procedures to be implemented in order to judge on auditor's report with regard to the type of fraud or misstatement, and the probability of fault occurrence or frau, and also his/her material effect on the financial statement
4. When the auditor detect material distortion due to fraud and misstatement then the auditor must inform the management and authorized personnel in the control positions or employees in the higher position inside the organization to take necessary actions against fraud or materials misstatement.
5. If the auditor concluded that it is not possible to continue in the auditing procedure because of fraud or illegal acts, then the auditor should aware his/her occupational and legal liability associated with special conditions of audit procedure and inform the body that appointed auditor to do the auditing task.
6. It is essential that the auditor to take responsibility for detection fraud and illegal acts in financial statements, because the potential risk of detection of fraud and illegal acts in the financial statements is higher than the risk of non-detectionof distortions resulting from material misstatements, and this mainly because fraud and illegal acts may be used in projects and complex plans, and managed very wellto hid fraud and illegal acts.
7. To work on auditing and examination of senior management that can overcome the control procedures and monitoring, as the ability of senior management to implement fraud and illegal acts,also avoidingorganization policies and control procedures because of their ability to influence the staff in the lower organizational levels through orders that instruct them to do illegal acts and fraudapparently or hidden.
8. The occupational organizations should develop standards and procedures that oblige the auditor to follow when auditing cases of disinformation and material misstatement in the financial statements
9. To pay high attention for professional and scientific qualifications of auditors and improve their performance through using modern technologies in doing their auditing job.
10. The occupational organization should specify the procedure and responsibilities of auditors accurately, and developing rules and regulations associated with distortion in the financial statements and their civil, legal, and criminal liabilities on them

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