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THE AUDITOR'S PROFICIENCY IN RECRUITING THE ANALYTICAL PROCEDURES FOR SERVING THE AUDITING JOB: AN APPLIED STUDY ON A SAMPLE OF INDUSTRIAL AND NON-INDUSTRIAL COMPANIES

Fatima Salih Mahdi
fatemaalgrban@uomustansiriyah.edu.iq
Accounting Department, College of administration and economics, Mustansiriyah University, Iraq.

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Abstract

The standard entrance "professional entrance" , which the international standards of Auditing and the professional standards that the (AICPA) has formulated, is regarded as the backbone on which auditors depend for recruiting the analytical procedures and serving the auditing process, in addition to the conventional auditing procedures. Accordingly, the present research comes into existence. It focuses on the importance of analytical procedures regardless of utilizing the quantitative samples such as ratios and indicators, or the analytical method via comparing time intervals or projects within the same activity.It is worth stating that the analytical procedures are so important for all stages of analytical work since they will be obligatory during the planning and reporting stage, and the auditor is free in utilizing them during the field-work stage. Thus it is necessary to shed light on the proficiency the auditor has concerning the selection of the most suitable procedure among the available ones during the suitable time and according to the activity under auditing.The (ALTMAN) method will be used in this research. This method will be applied to two companies: the first one is industrial and the other one is non-industrial. They represent the sample of the research to clarify theauditor's proficiency in his/her worksince having the experience is not enough, instead, the auditor must always seek to develop his scientific and practical skills. This is fulfilled via the permanent continuation of everything related to the profession in order to be able to fulfil the tasks assigned to him.

First Axis: Research Methodology

I. Research Problem: The problem of the research lies in the difficulty of an auditor's recognition of the importance of the analytical procedures in explaining the auditing-work results. This, in turn, is reflected on the results of the economic entity work which is under auditing, whether its activity has been industrial, agricultural, commercial, service,…etc.

II.Research Importance:

The research importance stems from the necessity that the auditor should possess technical skills concerning how to use the analytical procedures and recruit them in a way that serves the auditor's work results. This should be performed in a way that enables him depend on these results in analyzing any of the entity activities. What's more is that this enables him identify the causes of success of a certain activity or the failure of another within the same entity, or identifying the prominence of a certain entity and the failure of the others within the same activity, or the financial collapse of an economic entity during a certain year rather than the others.

III.Research Objectives:

The present research aims at:

1-proving how much the use of analytical procedures is important for the auditing-work fields.

2-increasingthe auditor's awareness and understanding of the role the analytical procedures play in the permanent improvingof the work-results.

3-clarifying the importance of the international standards in reinforcing the auditor's utilization of analytical procedures.

IV:Research Hypothesis

The research depends on the following hypothesis: if an auditor possesses enough experience concerning the use of analytical indicators and according to the industry kind that is subject to auditing, the results of his work will be more accurate and trustworthy, a matter that serves the whole auditing job.

Second Axis: Analytical Procedures-Theoretical Vision

I: Analytical Procedures- Concept in Auditing

The use of analytical procedures-methodsin auditing in the practical processes is referred to with various expressions. Chief among them are the Analytical Procedures , Analytical Auditing or Review, Business Approach to Auditing, or Performance Indicators Review. Generally speaking, there is an integrational relation between auditing procedures and analytical review-methods which are referred to as the Analytical Auditing Procedures. (Lutfi, 2007:538).

Auditing analytical procedures aim at utilizing quantitative types such as ratios, indicators,…etc., to identify or know certain accounts or results and then comparing them with the economic entity-reality which has been reviewed. After that, hypotheses are established for interpreting deviation and taking the suitable procedures for verifying them.

The analytical procedures have been used as complementary procedures for the traditional ones of auditing depending on the familiar standard or professional entrance that reflects the professional auditing standards established by the (AICPA), or the International Auditing Standards established by the International Union of Accountants. The International Standard No. (520) has stated that the auditor must apply the analytical procedures during the processes of planning and total overview for the auditing process. It is believed that analytical procedures may be applied in the other stages.

This Standard (520) has defined analytical procedures as the important ratios and indicators including the research results concerning the reversals and relations that are in contrast with the other related information or that that deviates from the amounts predictable. (Al-Mahayni, 2009:16).

Analytical procedures are also defined as the tests that are applied to financial data through a comparative study of the relations among these data or identifying how much the auditor depends on the basic tests throughout testing the details of processes or stocks using the analytical procedures and through combining them. (Abdul-Ridha, 2001:32).

They have also been defined as the financial informationevaluation that is made through studying the possible relations among the financial data on one hand, and between these financial data and the non-financial data on the other. This is done through comparing the registered values in records and the auditor's expectations.(Arens, 2003:289).

Depending on what has been presented above, it can be concluded that the auditing analytical procedures are the methods for getting new information via studying any relations that can be using in comparing any information . Financial analysis is useful for the steps of audit-planning as is shown by the International Standard No. (12) concerning the understanding of the customer's acts and identifying the possible risks. The application of analytical procedures may refer to aspects and forms of the customer's acts which the auditor has not been acquainted with before , and these procedures will help him identify the nature of the other auditing procedures , their timing andfield.

The (SAS 23) publication has made a list containing five auditing analytical procedureswhich are (Al-Mahayni,2009:17):

1-comparing the financial information with other comparable information during previous periods. This is done through utilizingthe time-series method for studying the development of the company performance-indicators within time intervals.

2-comparing the financial information with the evaluated information such as budgets and predictions: the planning budgets and predictions, that are placed by the economic entity administration concerning what its work- numbers should be, have been among the essentials in the universe nowadays especially in the economic entities that have big size. As a result, comparing the actual data with these data is considered as one of the most important methods of analytical auditing.

3-studying the relations between the financial information entities which can be acceptable in order to be used according to a predictable model formed upon personal experiences such as the relation betweentotal net profit and net sales. Here the auditor can estimate the value which this ratio should have depending on his personal experience and study the circumstances and environment of the economic entity under auditing. Later, he can compare it with the actual value to identify the possible deviations and studying their causes.

4-comparing the financial information with similar information related to industry which the economic entity works with: the other entities performance- indicators, that work in the same field "the same industry" and the same environment and their sizes are similar to those of the economic entity under auditing, can be made use ofin order to measure the entity performance.

5-studying the relations that exist between the financial and non-financial information that has a relation: the auditing process is a perfect one whether it is analytical or non-analytical. The auditor cannot only focus on the financial data and neglect the non-financial one.

The auditor uses the financial analysis (in all its forms)though the horizontal analysis is more suitable than the vertical one. Through his long period of studying the financial ratios within various years of the entity time, the auditor aims at identifying the deviations the occur in the elements of the financial lists. Here the horizontal comparison helps him in his first diagnosis. If he finds unexpectedor relatively great changes, then it is obligatory for him to make further examination and investigation. Accordingly, he must investigate the justifications for these changes (identifying what is positive and what is negative among them). He may also use the standard ratios wherever possible.

This analysis is very important and vital namely during the last stage of auditing which is called (critical or analytical audit), and as such his situation will be equal to that found in the Holy Quranic Verse (He said: Don't you believe? He said "Yes, but to reassure my heart). So the auditor is trying to get the ultimate satisfaction and reassurance concerning the results he has obtained during the various stages of his work. When studying the money ratio, for instance, the auditor may discover a concrete deviation different from the previous years or the approved standards. This leads him to seriously study the issue with much more attention to the account auditing that is represented by the identified ratio. As a result, it may be found that this has occurred due to a mistake in account, or in following a certain policy, or the sample that has been selected at the very beginning does not accurately represent the society. (Al-Hasany, 1998:416-17)

This auditing of accounts that is performed via the use of financial analysis is called (Analytical Audit). It is one of the auditing methods that the auditor resorts to identify or know the entity-special indicators as compared with previous time intervals or other similar economic entities which work in the same field. In his analytical audit, the auditor depends on identifying the expected value of any account according to the historical relations that link the financial lists with each other. The financial ratios represent the different relations between the elements of these lists and the different accounts to show the degree of connection or linkage among these elements . This means there ought to be a logical relation between the two terms that constitutethe ratio-components, a matter that gives it a certain significance.

Analytical procedures are considered as one of the essential examinations that the auditor makes use of mainly when making an auditing program. Here, he focuses on the terms that might contain essentialmistakes,as he thinks,, and as such , he asks for additional proofs when the controlling system is weak and cannot be depended on. (Jarboo', 2005:264).

II.Analytical Procedures: Objectives, Method and Types

1-The objectives of applying the analytical procedures in auditing:

Auditing the processes aims at (Abo Samhadanah, 2006:28-9):
a-understanding the economic entity-processes.
b-identifying the areas of risks.
c-evaluating the scope of testing the processes and balances.
d-identifying the fields or areas that require additional auditing.
e-verifying and reinforcing the audit results.
f-the total andthorough auditing of the financial information.

The auditor's aim behind the application of analytical procedures is represented by (Abdul-Righa,2001:37-9) and Al-maylem, 2003:6) :
i-analyzing the relationships between the financial and non-financial data to guarantee that these relations have no essential mistakes.
ii-reducing the detection risks that may depend on the primary audit-strategy and on the planning level of the fundamental tests.
iii-providing extra procedures after finishing the audit depending on the results obtained.

2-The method followed in executing the analytical procedures in auditing:

The auditor uses various methods for applying the analytical procedures. Among these methods are (ibid.:10):
i-Comparison Method:
The choice and use of the suitable analytical procedures are the most important step in the right application of this method. Some deviations that are expressed by risks and costs may result from the comparison processes. In order to fulfil the comparison, dependence may be made on the following:
a-Special comparison: that is fulfilled through comparing the financial information of the entity with the sector, market,…etc.
b-Internal comparison: that is essentially related to forming special comparisons concerning the same entity such as:
1-The indicators- value of the previous years. This is done through comparing the financial information of the current periods with the previous periods that precede it (Horizontal Analysis).
2-Comparing the relationships between the information and the results and the auditor's expectations (depending on his understanding ofthe entity-position and the procedures that are placed for it).
3-Studying the relationships between the financial informationand the concerned non-financial one such as (cost of wages and salaries with the number of workers).

ii-Statistical Method:

This method is regarded as one of the most commonly used methods in analytical procedures for evaluating and measuring how much the data and balances are reasonable through the linkage between the account through which the auditor wants to pass his judgement concerning its reasonability (dependent variable) and some other data (independent variable). A result that can be reached is that there are fundamental mistakes if there is a difference in the predicted value (a great difference as compared with the value apparent or found in the data and reports of the entity under audit). Therefore, it requires more specification and expansion in the auditing and examination process.

iii-Professional appreciation in Examination and Extracting the Results:

This method is used in case that the accurate methods formeasurement is unavailable or in the conditions of uncertainty of the results of the actions that are occurred or expected to occur. This requires personal judgement in the appreciation process and a high degree of specialized knowledge and judgement in case of complex appreciations. It is necessary here to pay close attention to the following aspects:

a-identifying the related elements that affect the accounting appreciation, andthe circumstances of the activity within which the entity works.

b-collecting suitable and enough data that are authentic.

c-a thorough knowledge of the internal system.

d-the consistency of the accounting appreciation which the entity has reached with its operational plans.

3-Types of Analytical Procedures Used by the Auditor:

Analytical procedures are regarded as one of the basic verifying tests- types that can be performed in order to collect the proofing evidences that are related to verifying the authenticity and suitability of the accounting treatment concerning the processes and balances, in addition to making sure that there are no mistakes or violations. (Lutfi,2007:542-3).

Analytical procedures include many types that the auditor uses according to his opinion concerning their suitability. There are many essential types such as (Nassar et al.,2008:15-20):

a-Comparing the data of the entity under audit with the activity data within which it works.

This type of analytical procedures helps in providing necessary information related to the performance of the audited entity. This is performed through comparing the difference between the nature of the entity financial information under auditing with the data that represent that total of the activity of the other entities. This comparison helps the audit understand the entity work, let alone it offers an indicator of a financial failure if there is any.

b-Comparing the data of the entity under auditing with the equivalent data during previous periods.

Within this type, the auditor compares the ratios and financial indicators of the entity under auditing for the previous years with the ratios and financial indicators of the entity for the ongoingfinancial year. If an increase or decrease is noticed in one of these ratios and indicators, the auditor must predict the causes that may lead to this increase or decrease depending on his experience, and then, he must find the proofs, collect them in order to make sure of these probabilities.

c-Comparing the data of the audited entity with their expectations.

This type of analytical procedures is applied in auditing concerning the Governmental Units. Most entities prepare estimated budgets for the accounting periods and then comparing them with the actual data. If a difference exists between the two types of data, this means that there are changes that require searching for their reasons on the part of the auditor and be convinced with them. Also, he must make sure of whether the entity has remodified the data in the estimated budgets that affect the nature of these budgets , which in turn, affects the analytical procedures-results and how much they are depended upon.

d-Comparing the entity data under auditing with the auditor's expectations.

In this type of analytical procedures, the auditor performs some calculations to get expected values of some balances in the financial lists. This is usually done according to some historical trends for these balances. After that he compares the results of these analytical procedures with the entity data and then he can identify the balances that require examination and collecting evidences concerning them.

e-Comparing the entity data under auditing with the results via the use of financial and non-financial data.

This type is used to ensure the balances or appreciate some of them. The auditor cannot depend on this type of analytical procedures unless he is sure of the accuracy of the non-financial data.

Third Axis: Taking Advantage of the Analytical Procedures in Auditing

First: Advantages of the use of Analytical Procedures in Auditing

Generally speaking, analytical procedures have great advantages for the auditor during all audit-stages. These advantages are (Al-Thunaibat,2009:207):

1-Enabling the auditor understand the client's work through comparing his financial ratios with the other institutions in the industry in which he works.

2-They can direct the auditor towards some financial problems that the client faces.

3-Enabling the auditor appreciate the client's ability of continuity or progress.

4-They may pay the auditor's attention towards deviations found in accounts.

5-They may lead to reducing the size of the elaborated tests.

6-They enable the auditor compose the final image of the client's financial data.

Second: International Standards- Affirmations on the Use of Analytical Procedures in Auditing

International Standards are considered the director or guidance in auditing. In the Standard No. (520), it has been clarified previously that the aim behind this Standard is to place standards and provide guidance concerning the application of the analytical procedures during the audit-process. For instance, the analytical procedures include a comparative study of economic financial entity-information with (Accountants International Union, 2007:459):

1-The comparable information of the previous periods.

2-The expected results such as (estimated budgets, predictions, or the auditor’s expectations such as estimating the consumption.

The information identical to the sectoral entity such as comparing the rate of the entity sales with its accounts, under collection, with the relevant averages in the sector or with other projects in the same sector that have similar sizes.

Analytical procedures also include studying the relations:

a-between elements of the financial information that are expected to be similar to the predictable model that is built upon the company experience such as the percentages of the gross profit margin.

b-between the financial and non-financial information that has a relation. It is possible to use various methods to fulfil the above procedures. These procedures stretch from the simple comparisons till the complex analyses that use advanced statistical techniques. Analytical procedures can be applied to the unified financial data or the partnerships-data such as subsidiary companies, departments or sectors, or in the separate elements in the financial information.

The auditor’s choice of the procedures, methods and the level of application depends on his operational judgement. The International Standard No. (520) has shown that the analytical audit is the process of checking the information found in the accounts and records of the entity and then comparing it with other information and the internal and external data in order to come up with an opinion concerning how harmonic this information is with what is known about this entity and its activities.

Analytical audit is also defined as the analysis of relationships between the financial and non-financial lists of the same period and then comparing them with the financial and non-financial information of other periods. This is performedin order to identify the homogeneity between information and any differences, fluctuations or unexpected relationships, and then coming up with a result concerning these tests. The auditors usually reform the previous definition in a form of a question that states “Do the figures make sense in the light of what the auditor has found out about the organization?”

The aim of analytical audit in any of the auditing stages, in which the auditor looks for evidences, is directing the auditor towards the required evidences that enable him come up with the results concerning the audit and pass his opinion. Accordingly, the process of analytical audit of accounts should not be assigned to the individuals who lack these abilities because this will make the audit process more expensive and less useful.

The skills of utilizing analytical audit-methods in addition to the other methods are the process of accurately directing the resources towards their correct position, a matter that reduces costs, improve efficiency and saving time. The points that should be taken into account when making analytical audit are as follows:

1-An overall review: at first, the auditor should make a general test for the financial data before starting the analytical procedures in order to clarify all the points. This helps him use the financial ratios correctly and placing them in their correct position.

2-Financial ratios are just mere tools, or relations that are formulated in the form of ratios. So to be useful, they must be compared with:
●-Previous years-ratios
●-The expected ratios as in budgets.
●-The various parts of the activity.
●-The other entity and industry.
These procedures enable the auditor identify the preferable and non-preferabledeviations and know their reasons.
3-The need for combining the ratios with each other: financial ratios should be taken apart from each other. For instance the money ratios should be explained within the frame or area of activity ratios.
4-Taking enough time and adequate caution when explaining the analysis results. It is important to pay attention to the contriving of the evidences out of the analytical procedures. The auditor must be able to get the reinforcing evidences that support the analysis results. It is mistaken to consider the figures as being correct just by looking at the relation among them. Linking, comparisons and using reinforcing evidences should be made. (Al-Thunaibat, 2009:203-6).

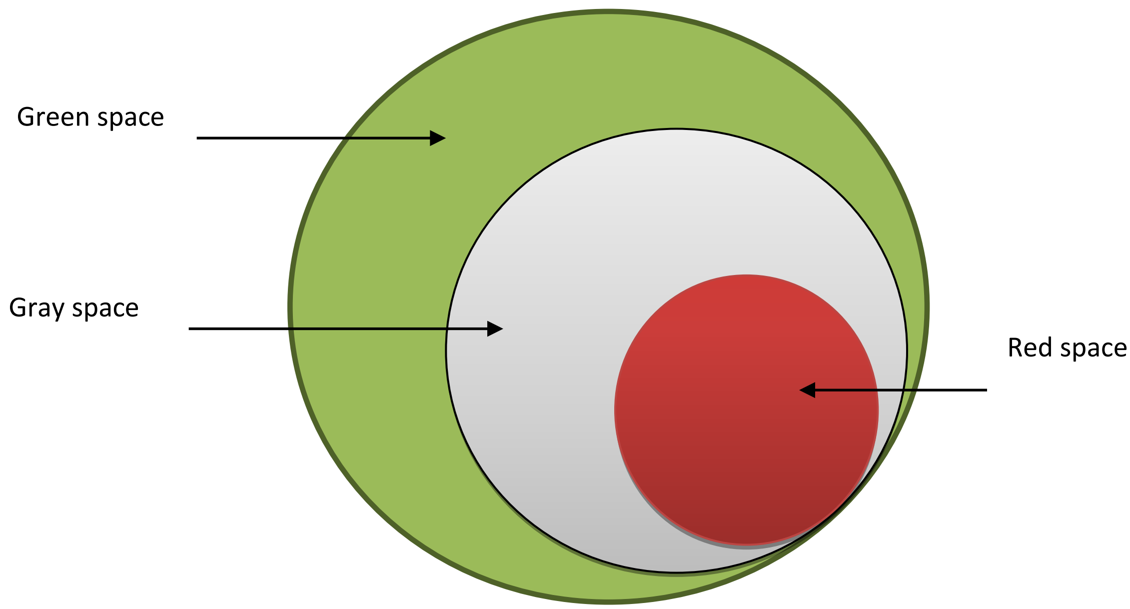
Fourth Axis: Practical Part
First: Research Sample
Analytical procedures of two companies will be compared.One of them is industrial while the other is not. To hide the two companies-data and names, a symbol will be used for this purpose. As such, the industrial company will be symbolized as (S), and the non-industrial as (X). The auditor can discover, through the use of analytical procedures namely the percentages of both companies-data, which one of them may have risks, financial failure or creative accounting as a kind of manipulation of the company accounts.
Both companies will be studied for one year, i.e. (2016) which is regarded asone of the years that witnessed a kind of constancy concerning supply, demand, prices or the external influences such as the economic, social and political position. The data that the auditor needs have all been there for both companies and they have been verified by the auditor as well.
To clarify the areas divided and named by scientists when the companyis vulnerable to failure, financial collapse, bankruptcy or dissolution, or when it has invalid future or is in its best position at present or in future, and in order to predict whether there are some attempts for the creative accounting, the (Altman) Model will be depended upon. Through this model some financial ratios can be obtained and identifying such attempts mentioned above.Companies are classified into three types depending on this model. They are as follows:
1-Red zone: if the model result is less than 1.8 ($z< 1.8$).
2-Foggy zone: if the model result is at about (1.9-2.9) ($2.9<z<1.9$).
3-Green zone: if the model result is greater than 2.9 ($z>2.9$)
Second: Altman Application to the Industrial Co. (S)
The formula of this model in the industrial companies is as follows:

$Z= 1.2*X1+1.4*X2+3.3*X3+0.6*X4+1.0*X5$
Since:
X1= working capital ÷ total assets
X2= retained earnings (profits) ÷ total assets
X3=profits before benefit and tax ÷ total assets
X4= market-value of equity ÷ total liabilities
X5= net sales ÷ total assets
If we take this model (Altman) and apply it to the industrial company data (S), we will get:
X1=0.652
X2=0.006
X3=0.065
X4=0.685
X5=0.323
$Z=1.2*0.652+1.4*0.006+3.3*0.065+0.6*0.685+1.0*0.323$
$Z=0.7824+0.0084+0.2145+0.411+0.323$
$Z= 1.7393$
Going back to the classification of companies according to the previous model, it can be noticed thatZ= 1.7393 which lies in the red zone. So when it is (Z< 1.8), this classifies the company within the type that lies within the red zone. This has been explained as that the company may face the risks of financial failure, bankruptcy or dissolution.

Third: Altman Model Application to the Non-Industrial Co. (X)

The formula of this model for the non-industrial companies is as follows:
$Z= 1.2*X1+1.4*X2+3.3*X3+0.6*X4$
Since:
X1= working capital ÷ total assets
X2= retained earnings (profits) ÷ total assets
X3=profits before benefit and tax ÷ total assets
X4= market-value of equity ÷ total liabilities
Taking this (Altman Model) specialized for the non-industrial companiesand applying it to their datawill result in:
X1=0.115
X2=0.008
X3=0.027
X4=0.58
$Z= 1.2*0.115+1.4*0.008+3.3*0.027+0.6*0.58$
$Z=0.138+0.0112+0.0891+0.348$
$Z=0.5863$
If we go back to the companies- classification according to the previous model, it is noticed that (Z=0.5863), this lies within the red zone. When the(Z< 1.8), this classifies the company under the type that lies within the red zone. This is explained as that the non- industrial company is exposed to threats such as the financial failure. The following scheme No. (1) clarifies this:

Economic Entity



The chart is the researcher's own made.

Accordingly, the analytical procedures with their various uses have a great effect in providing a vivid picture concerning the company under audit. Here, the auditor, depending on his own experience can have a simple satisfaction that he is able to make logical analysis of the activities of any company under audit whether it is industrial or non. Through the accurate examination he has got the results related to the work of the company as a whole, let alone the information concerning its near future.As a result, this emphasizes that the auditor has the skills that he can use in his audit, but here intelligence and insight play the central role in choosing the most suitable method to turn this skill into an auditor's innovation.

Fifth Axis: Conclusions and Recommendations

First: Conclusions

1-There is an integrative relation between audit- procedures and analytical examination-methods. It can be expressed by the term (Analytical Auditing-Procedures).

2-Practical experience alone is not enough for the auditor in his work, instead, he must keep following up with everything related to his job such as reviews, periodicals, international standards and publicationsconcerning his job.

3-The International Standard No. (520) has emphasized the importance of analytical procedures for the auditor during the audit-stages. The Standard has given liberty for the auditor in choosing the most suitable procedure in fulfilling his audit.

4-Horizontal analysis is considered as more suitable than the vertical one in studying the relationships between different data of the same company within two different periods, or the data for two different companies within the same activity and the same period as well.

5-The auditor uses various methods through which he aims at executing the analytical procedures such as Comparison Method, Statistical Method, and the Professional Appreciation in Examination.
6-The auditor's opinion depends on facts which he reaches via proofing evidences that he gets through the various audit-working stages which represent the guidance for the auditor to fulfil the aims of analytical audit.
7-If the auditor has the ability to recruit the analytical procedures and makes use of them to obtain important results related the nature and quality of the activity under audit and are related to future risks that may lead to financial losses or collapse, or may reflect the misuse of profits or dissolution, here, he has utilized all his skills for the sake of his job and thisis the ultimate thing.

Second: Recommendations

1-Depending on his own experience and notions that he has got throughout his work-stage, the auditor should create the integration between the available auditing procedures and the methods of analytical examination in order to obtain satisfactory results related to the whole audit process.
2-The auditor should make a kind of parallelism "balance" between the academic and practical efficiency to trim his academic knowledge with his practical experience. This is done depending on the recent developments in the International Standards to be up to the responsibility for executing all the jobs assigned for him.
3-Within their companies and offices, it is so important for t auditors to pay close attention to the International Standards especially the Standard No. (520) which is considered as a road map that guides them towards choosing the most suitable procedure or method among the other ones.
4-Among his duties, the auditor should use all the forms of the financial analysis, to serve the whole audit-process, whetherit is the horizontal or vertical analysis or the ratios- method.
5-The auditor should select the statistical method among the other methods available because this method is the most common one for executing analytical procedures and it provides reasonable results via linking the dependent variable with the independent one.
6-The process or job of analytical audit of accounts should not be assigned to inefficient or non-professional auditors because this will make the audit more expensive and less useful.
7-It is necessary for any efficient auditor to usefully use the analytical procedures within any stage of work. This will be reflected on providing a thorough vivid picture about the company position under audit and the crises which it may face at present or in future.

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