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THE ASSESSMENT OF INDEPENDENT EXTERNAL AUDITING PERFORMED IN TURKEY IN TERMS OF GENERALLY ACCEPTED AUDITING STANDARDS

Şerife MUTLU DUMAN

Danışman
Doç. Dr. Banu Esra ASLANERTİK

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Yüksek Lisans Tezi olarak sunduğum "The Assessment of Independent External Audıtıng Performed In Turkey In Terms of Generally Accepted Audıtıng Standards" adlı çalışmanın, tarafımdan, bilimsel ahlak ve geleneklere aykırı düşecek bir yardıma başvurmaksızın yazıldığını ve yararlandığım eserlerin kaynakçada gösterilenlerden oluştuğunu, bunlara atıf yapılarak yararlanılmış olduğunu belirtir ve bunu onurumla doğrularım.

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FOREWORD

I would like to thank you to my advisor Associate Professor Banu Esra ASLANERTİK for her important support during the writing process. I also thank to my friends Desen and Mustafa YAMAN, Seda IŞIK, Bahar ÖZKAN and Duygu YAŞA for their kind support and of course to my family especially to my husband Vural DUMAN for his everlasting belief.

ÖZET

Yüksek Lisans Tezi

Türkiye'de Yapılan Bağımsız Dış Denetimin Genel Kabul Görmüş Denetim Standartları Açısından Değerlendirilmesi

Şerife MUTLU DUMAN

Dokuz Eylül Üniversitesi
Sosyal Bilimler Enstitüsü
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Son yıllarda, dünyada ve Türkiye'de yaşanan denetim skandalları şeffaf finansal tabloların oluşturulması ve finansal tablo kullanıcılarının bu tablolara olan güveninin sağlanması açısından bağımsız dış denetimin önemini daha iyi göstermiştir.

Dış denetim çalışmalarının yeterliliği ve kalitesi ancak bazı kıstasların geliştirilmesi ile sağlanabilmektedir. Bu kıstaslar denetim standartlarıdır. Çok az değişikliğe uğrayarak günümüze kadar gelen "Genel Kabul Görmüş Denetim Standartları" (GKGDS) denetim faaliyetleri açısından uyulması gereken asgari standartlardır.

Bu çalışmanın amacı, Türkiye' de sermaye piyasası mevzuatı, mali müşavirler ve yeminli mali müşavirler mevzuatı ve bankacılık mevzuatı kapsamında bağımsız dış denetime ilişkin yapılan düzenlemelerin GKGDS ile ne derece uyumlu olduğu konusunda bir kanaate varmaktır.

Yapılan inceleme neticesinde, Türkiye'de sermaye piyasası mevzuatı çerçevesinde bağımsız dış denetime ilişkin yapılan düzenlemelerin GKGDS ile uyumlu olduğu, bankacılık mevzuatı çerçevesinde yapılan düzenlemelerin ise sermaye piyasasında yapılanlar kadar olmasa da GKGDS ile paralel olduğu sonucuna varılmıştır. Ancak mali müşavirler ve yeminli mali müşavirler mevzuatı çerçevesinde yapılan düzenlemelerin GKGDS'nı karşılamaktan uzak olduğu görülmüştür.

<u>Anahtar Kelimeler:</u> **1**)Denetim, **2**) Bağımsız Dış Denetim, **3**) Genel Kabul Görmüş Denetim Standartları

ABSTRACT

Master Thesis

The Assessment of Independent External Auditing Performed in Turkey in Terms of Generally Accepted Auditing Standards

Şerife MUTLU DUMAN

Dokuz Eylül University
Institute of Social Sciences
Department of Business Administration (English)

Audit scandals experienced recently in world and in Turkey have better shown the importance of independent external audit in the sense of producing transparent financial statements and earning confidence of financial statement users.

Competence and quality of external audit can be guaranteed only when certain criteria are developed. These criteria are auditing standards. "Generally Accepted Auditing Standards (GAAS)" that have reached today with very few changes are the minimum standards required to be followed during audit activities.

The aim of this study is to reach a conclusion on the extent to which the arrangements in Turkey concerning independent external audit within the scope of the legislations on capital market, certified public accountancy and sworn-in certified public accountancy and banking comply with GAAS.

Following the study, it is concluded that arrangements regarding independent external audit in Turkey within the capital markets legislation comply with GAASs, while those within the banking legislation are in parallel with GAASs, though not as much as capital market's arrangements. However, arrangements made within the frame of the certified public accountancy and sworn-in certified public accountancy legislation are far from meeting GAASs.

Key Words: 1) Auditing**, 2)** Independent External Auditing, **3)** Generally Accepted Auditing Standards

TABLE OF CONTENTS

THE ASSESSMENT OF INDEPENDENT EXTERNAL AUDIT PERFORMED IN TURKEY IN TERMS OF GENERALLY ACCEPTED AUDITING STANDARDS

SECTION II

GENERALLY ACCEPTED AUDITING STANDARDS

SECTION III

THE COMPARISON OF INDEPENDENT EXTERNAL AUDIT PERFORMED IN TURKEY WITH GENERALLY ACCEPTED AUDITING STANDARDS

ABBREVIATIONS

AAA	American Accounting Association
AICPA	American Institute of Certified Public Accountants
ASB	Auditing Standard Board
BRSA	Banking Regulation and Supervision Agency
CMB	Capital Market Board
CPA	Certified Public Accountants
EEC	European Economic Community
EU	European Union
GAAP	Generally Accepted Accounting Principles
GAAS	Generally Accepted Auditing Standards
FASB	Financial Accounting Standards Board
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards
PCAOB	Public Company Accounting Oversight Board
SAS	Statements on Auditing Standards
SEC	Securities Exchange Commission
TMUDESK	Turkish Accounting and Auditing Standards Board
TÜDESK	Turkish Auditing Standards Board
TÜRMOB	Union of Chambers of Certified Public Accountants of Turkey

FIGURES

INTRODUCTION

In an environment where technological developments and globalization dominate on an international scale, flourishing and complexifying economic life boost the need of accessing reliable information. However, it is nearly impossible for the decision-makers to reach the information at first hand. When obtained from other persons, the likelihood of intentional or unintentional misstatement, on the other hand increases. Particularly if there is a conflict of interest between the decision-maker and the source arranging the information, there arises risk of losing impartiality to information providing source.

The fact that information declared is not sufficiently reliable forces the decision-makers to take certain precautions in this regard. In advanced economies, it is detected through independent external audit whether or not the information declared by companies with respect to their financial statements to interest groups is reliable.

Various interest groups using results of independent external audit might not have adequate information and abilities or time; therefore, it is not always possible for them to make assessment on the quality of audit services provided. There are minimum requirements that must be observed by the members of the profession from the aspects of both the audit quality assurance and inspiring public confidence in the work done and in auditor opinion. "Generally Accepted Auditing Standards" approved at international level satisfy this need. These standards specify in general terms the professional qualifications an auditor must hold, activities that must be performed during audit practice and the rules to be observed in reporting. (Kavut, 2000; 9-10)

Arrangements on independent external audit in Turkey are made by laws, in contrast to developed countries where there are professional associations regulating audit. Despite the fact that Turkish Auditing Standards Board was established in 2003 with the purpose of setting and issuing national auditing standards, said Board has not established the standards, but just translated the international auditing standards to Turkish. With a view to determining auditing standards by single authority and establishing public oversight system, a draft law on “Turkish Auditing Standards and Public Oversight Authority” was submitted to the Parliament in 2008, which has not been enacted yet. For this reason, arrangements and standards in the area of independent external audit in Turkey are still regulated within the framework of different legislations.

This study explores, under three Parts, to what extent the arrangements in Turkey concerning independent external audit within the scope of the legislations on capital market, certified public accountancy and sworn-in certified public accountancy and banking comply with GAAS.

First Part of the study defines the concepts of audit and independent external audit, and touches on the significance and development of audit.

What follows in the second Part are the issues of Generally Accepted Auditing Standards, developments in audit and auditing standards in Turkey and Associations having role in auditing standards both in Turkey and in the world.

Finally, the third Part of the study analyzes each Generally Accepted Auditing Standards with the main lines and specifies to what extent the arrangements in Turkey concerning independent external audit within the scope of the legislations on capital market, certified public accountancy and sworn-in certified public accountancy and banking comply with GAAS.

SECTION I

GENERAL DEFINITION OF AUDITING AND INDEPENDENT EXTERNAL AUDITING

1.1 Conditions Creating Demand for Auditing

Growth of society, gradually getting more complicated of economic life is increasing the need for reliable information. Information being utilized should be accurate and reliable in order to make objective, suited and consistent decisions. Unreliable information harms society and decision maker by preventing the efficient usage of resources. However, as society becomes more complex, there is an increased probability that unreliable information will be provided to decision makers. (Güredin, 1997: 1-2) There are many obstacles in front of obtaining reliable information. Some of them are as follows: (Hermanson et al., 1976: 4-5)

Conflict of interest: Users are concerned with the possibility of bias in the information provided when there is an actual or potential conflict of interest.

Consequence: When information is used as input for decision of significant consequence, users are concerned with the possibility of biased, misleading, or incomplete information could lead to incorrect decisions which are harmful to the user or those significantly influenced by such decisions.

Complexity: As information communicated has become more complex, users of information have found it more difficult or even impossible to obtain direct assurance as to the quality of the information received. Also, as the subject matter becomes more complex, the possibility of unintentional errors creeping into the information increases.

Remoteness: Remoteness is occurred when the user of the information and information sources were separated and this prevents the user from directly assessing the quality of information received.

Accurate and reliable information forms the basics of a healthy decision making process. In this phase, negativities told above become greatest obstacles in front of a decision maker. Decision maker somehow should search whether the information that will be used in decision-making process is reliable or not. A common method applied in checking whether the information announced is sufficiently reliable is to audit and attestation of this information by an independent person. (Güredin, 1997: 2)

Credibility added to the information by independent persons reduces the decision maker's information risk. (Whittington and Pany, 2001: 6) Since, the audited information, used in decision-making process, is accepted as reasonably complete, accurate, and unbiased. (Arens and Loebbecke, 1976: 3)

1.2 General Definition of Auditing

The American Accounting Association Committee on Basic Auditing Concepts has defined auditing as follows:

"Auditing is a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic action and events to ascertain the degree of correspondence between those assertions and established criteria and communicating the results to interested users."

This definition includes several key words and phrases that require further explanation. The phrase *systematic process* means that auditing is a logical, purposeful, and structured approach to decision making; it is not an unplanned, haphazard process. (Guy et al., 1999: 5)

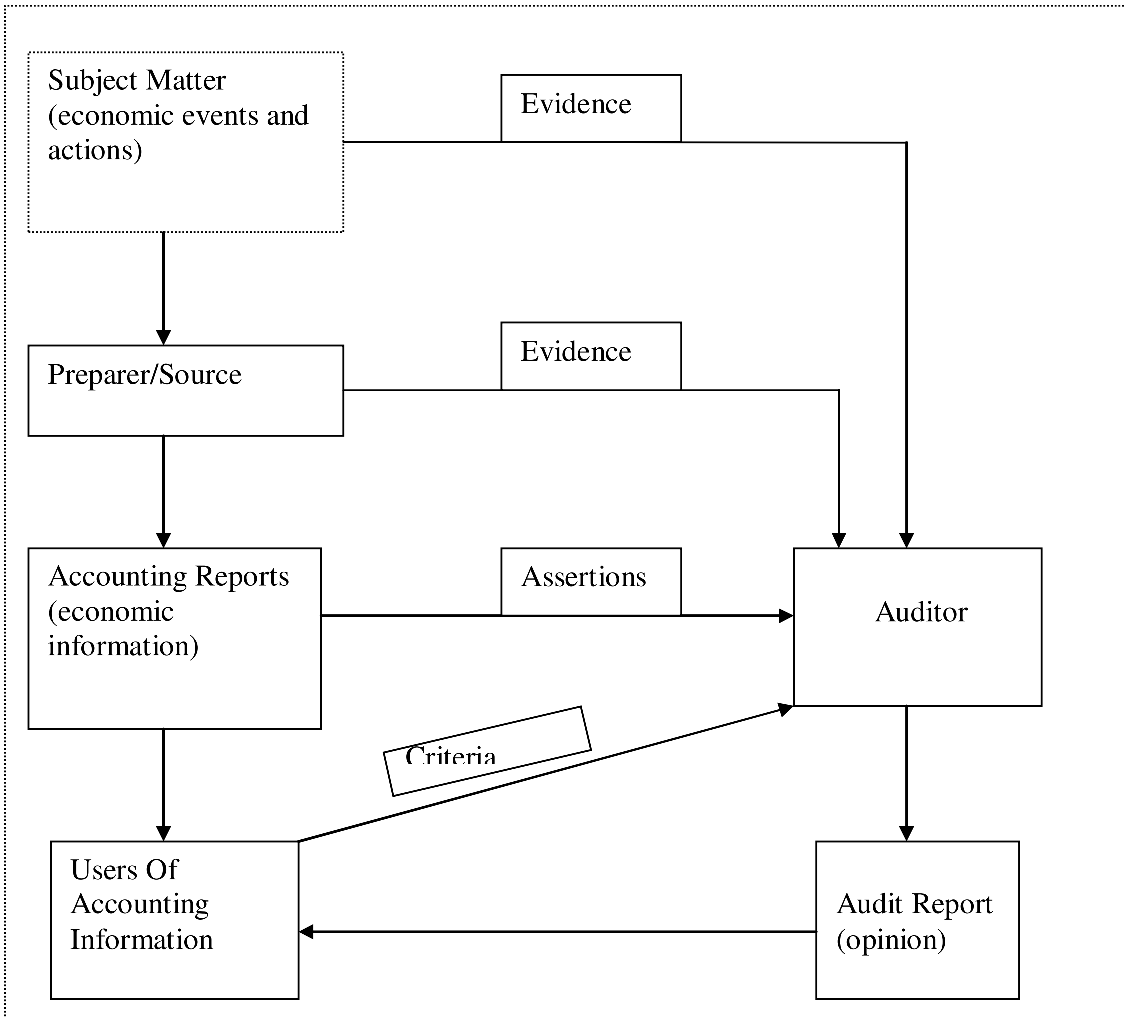
Objectively obtaining and evaluating evidence statement implies that auditing involves the collection of evidence. Evidence represents information that will affect the auditor decision making process. Evidence takes many different forms, such as examination of documents, observations by the auditor, and confirmations of balances from third parties. The process of collecting and evaluating evidence must be as objective as possible. (Guy et al., 1999: 6)

Assertions about economic actions and events phrase means that a basic component of auditing process is the collection of evidence regarding assertions about economic actions and events. These assertions often relate to the financial statements. The auditor is given financial information and financial statements by the auditee, when conducting a financial statement audit. These financial statements represent the auditee's assertions about economic actions and events and include not only the financial statements themselves but also the accounting information system and the accounting process. (Guy et al., 1999: 6)

To assess *the degree of correspondence between assertions and established criteria* the auditor compares the evidence gathered to assertions about economic activity. Although there are many sets of criteria for measuring the degree of correspondence, generally accepted accounting principles are usually used for preparation of financial statement. (Messeir, 1997: 9)

The last phrase *communicating results to interested users* is concerned with the type of report the auditor provides to intended users. The intended users may include stockholders, debt holders, employees, suppliers, government agencies, stock exchanges, and other groups. (Messeir, 1997: 9)

The Figure 1.1 Graphically Shows an Overview of the Audit Function



(Source: Silvoso et al., 1972: 27)

1.3 Historical Development of Auditing

Development phases of auditing profession can be divided as; before and after “Industrial Revolution”. Although the auditing did not have a formal structure before Industrial Revolution, its application goes quite back. (Ataman et al., 2001: 16). In tablets belonging two thousand years ago and inscriptions at the ancient city remaining showed, that audit of public expenditures was performed in Egypt, Rome and Greek civilizations. (Porter et al., 1996: 169)

In early times, auditing techniques consisted almost exclusively of a detailed verification of every transaction, which had taken place. As an audit procedure, the concept of testing or sampling was unknown. (Brown, 1962: 697) Also, from medieval times to the Industrial Revolution, audits were performed to determine whether persons in positions of official responsibility in government or commerce were acting and reporting in an honest manner. (Whittington and Pany, 2001: 8)

The Industrial Revolution was a primary incentive for the auditing profession. During the nineteenth century companies expanded facilities, changed production methods, and created complex organizational structures. One result was that owners became less involved in directing their enterprises, assigning that function to professional managers. This separation of ownership from management increased the demand for auditing because the biases and motives of managers in some respects differed from those of owners. During the Industrial Revolution, the audit’s primary purpose was to detect fraud and to assess the stewardship of managers for the stockholders. A significant event for auditors was the passage of the Companies Act of 1862 in Great Britain, which required corporations or stock companies to have independent audits. (Guy et al., 1999: 8)

In the first half of the 20th century, the direction of audit work tended to move away from fraud detection to a new goal of determining whether financial statements gave a full and fair picture of financial position, operating results, and changes in financial position. This shift as a response to the increasing number of shareholders.

In addition to shareholders, auditors become more responsible to governmental agencies, new investors, as well as other parties who might rely upon the financial information. (Whittington and Pany, 2001: 8-9)

In 1940's and 1950's two significant changes occurred in the audit approach. First, emphasis of financial statement users shifted more to income statement and away from the balance sheet and the auditor's objective move accordingly. The second major change that occurred in auditing during this period was the increasing emphasis on the review of internal control as the key to audit. As a collar of this change, concepts of sampling came to be more frequently used. (Porter and Burton, 1971: 78)

Within 1960-1990, usage of evidences in audit process provided from external sources is highlighted. Towards 1990's it was seen that computers were also used in audit process. At the same time, collection of evidence by using statistically sampling method is more commonly used. Development of data processing systems in 1990's and increase of enterprises' global activities caused the predomination of a new audit concept. In this phase, field of audit expanded and the auditors began to contribute enterprises' management action. In audit process, usage of statistical and mathematical methods (sampling method) preponderated and also examination of informatics infrastructure of audited enterprises outshined. With various software developed in this term, computer programs were also utilized in auditing. (Porter et al., 1996: 27)

Nowadays, whether experienced corruption scandals or the need of using the auditing sources ideally highlighted the fact of "risk focused audit". In "risk focused audit" approach, risks of enterprises are analyzed in details. Audit is performed by using the determinants brought out in the lights of data's obtained by risk analyses. Audit is performed more effectively by courtesy of "risk focused audit". Owing to this, more effective usage of sources in audit process is required. (Porter et al., 1996: 27

1.3.1 Development of Audit in England

In modern sense, external auditing was first applied in England at the beginning of 19th century. Expansion of production capacity increased accounting operations and this caused the need of account operations' approval to check their accuracy. For this purpose, in 1845 audit of railway companies' balance sheets were required by laws. (Aksoy, 2002: 85)

England is the first place where independent auditing institutions were legally seen besides the implementation of external audit. In 1880, The Institute of Chartered Accountants in England and Wales was founded by coalition of five local accounting groups. (Çarıkçıoğlu, 1995: 149)

Emergency of auditing of account as a compulsory by independent auditors happened again in England in 1900 with making it an obligation for limited companies. (Havan, 2006; 48)

Delivering true and impartial opinion is a rule which forms the basics of England accounting principles and is really cared out. There are five main accounting organs in England. (Akgül, 2000: 22)

-The Institute of Chartered Accountants in England and Wales
-The Association of Certified Accountants
-The Institute of Cost and Management Accountants
-The Chartered Institute of Public Finance and Accountancy
-The Institute of Chartered Accountants in Ireland
-Consultative Committee on Accountancy Bodies

Institutions have important role as adoption of accounting principles in England, implementation of countrywide and audit of partnerships. According to England Corporate Law, all trade and industrial institutions must have audited by the members of The Institute of Chartered Accountants in England and Wales. England

Finance Ministry and Tax Administration closely collaborate with professional associations especially in financial range. (Aksoy, 2002: 87)

1.3.2 Development of Audit in USA

Audit profession of accounting and enterprise in United States of America formed and developed parallel with England. Enterprises are audited in terms of tax laws and auditors tried to establish particular standards in enterprises in USA where the first auditing system was founded in 1778. (Akgül, 2000: 24)

Studies for regulating the accountant profession in USA began with the foundation of American Association of Public Accountants in 1887. (Aksoy, 2002: 87) In the same year first Law of Certified Accountant Experts is accepted. (Havan, 2006: 49) With the foundation of semi-official American Institute of Certified Public Accountants (AICPA), spread of generally accepted accounting principles and creation of standards in external auditing are provided. (Beyazıtlı, 1991: 154)

In 1936, American Accounting Association (AAA) was founded and financed the accounting researches. In 1939 Committee on Auditing Procedure took office to establish the procedures concerning auditing. Standards concerning external auditing were first published by AICPA with the name "Generally Accepted Auditing Standards" in 1947. (Beyazıtlı, 1991: 165)

In America, Financial Accounting Standards Board (FASB), semi-official and independent from AICPA, was founded in 1973. FASB being founded independently from AICPA affected AICPA's role and AICPA gave up rule establisher role. However, in independent external auditing, the only rule establisher is still AICPA. (Dönmez, 2002: 23)

AICPA made it obligatory to obey the Generally Accepted Auditing Standards with "Code of Professional Ethics" issued in 1981. (Havan, 2006: 49)

1.3.3 Development of Independent External Audit in France

Legal regulation of accounting and auditing profession in France began with "Certificate of Expert Accountant" in 1927. (Akgül, 2002: 19). In 1942, "National Union of Expert and Authorized Accountants" was founded. Later with a governmental decree in 1945, distinction of Expert Accountant and Authorized Accountant gained a legal basis. In 1970's authorized accountant group is totally abolished by governmental decrees. (Çarıkçıoğlu, 2006: 149)

In a governmental decree dated 1976, expert accountant is described as "a person authorized to audit and assess an enterprise independently". To be an expert accountant, they should get certificate of expert accountant, which is given by French National Education. To get this certificate, success in two different examinations and getting experienced by working with an expert accountant for two years are required. (Solakoğlu, 1991: 65)

Accountant profession in France is divided in two groups; Expert Comptable and Comptable Agres. Expert Comptable are people who work independently, analyze enterprises financially, perform account audit, set accounting organizations and make declaration about the accuracy and impartiality of financial statements. Comptable Agres are people who work independently, carry out the accounting operations and make declaration about the accuracy and impartiality of financial statements of enterprises with which they deal with. (Akgül, 2000: 19)

In France profession institution concerning auditors is Union of Expert Accountants. (da la Compagnie Nationale des Commissaires) Auditors have to be members of it. (Akgül, 2000: 19)

1.3.4 Development of Audit in Germany

In Germany administration of auditors (Wirtschaftprüfer) is carried out by The Chamber of Auditors which founded in 1928. (Çarıkçıoğlu, 2006: 150). The

Chamber of Auditors works under the custody of Economy Ministry. Chamber protects the rights and benefits of its members besides auditing their work and activities. (Aksoy, 2002: 90)

"Profession Organization Law" which re-regulates the profession of enterprise auditors and auditors and founds the Chamber of Enterprise Experts in Germany was established in 1943. Today profession of enterprise auditors and account auditors is carried out according to the Organization of Enterprise Auditor Profession Law established in 1961.(Akgül, 2000: 19)

In Germany, tax consultation profession is organized in 1973. Profession of tax consultation is organized locally and chambers compose Federal Chamber of Tax Consultants. (Akgül, 2000: 20)

In Germany, auditors also provide some services like, tax consultation, legal consultation, and representation of clients in tax organs, besides auditing services. (Çarıkçıoğlu, 2006: 150). In the external audit system of Germany, not only enterprises with conventional personality but also real personalities are audited. (Akgül, 2000: 20)

1.3.5 Development of Audit in European Union

EEC, founded in 1957 with the name of European Economic Community (EEC), renamed as European Community (EC) in 1987 and then as European Union (EU), began working for establishing a common law order and provides coherence between laws of all member countries. (Aksoy, 2002: 91)

Before the foundation of European Community, in 1951 European Union of Accountants was founded with the goal of providing coherence and cooperation in accounting between European countries and developing uniform accounting implementations. Australia, Belgium, France, Germany, Holland, Italy, Luxemburg, Portugal, Spain and Switzerland were founder members. England and Holland joined the foundation in 1963. (Aksoy, 2002: 91)

EU is trying to provide coherence between the national differences in member countries' legal and economic structures with the help of directives published. However, this coherence can be realized if member countries adapt these published directives to their national laws. EU, acts only as an advisor, has no power to make legislation in member countries. But member countries have to obey these instructions by changing their laws and regulations in a particular time. (Dönmez, 2002: 25)

EU has published 4th, 7th and 8th directives concerning accounting and auditing until today. The Fourth Directive accepted in 1978 is the first important regulation of company law. Directive bought regulation about financial statements, annual accounts, assessment principles and audit topics in personal and public open corporations. (ICEE; Directive No: 78/660, 25.06.1978)

The Seventh Directive, which concerns consolidated financial statements, was accepted in 1983. Directive includes consolidated financial statements, explanatory notes, publish and audit of annual activity reports. (ICEE; Directive No: 83/349, 13.07.1983)

Compulsory audit standards by European Union were determined in Eighth Directive published in April 10th 1984. Goals of this Directive are, meeting the needs of people working as legal auditor and providing the harmonization of European Union member countries' auditing standards with Generally Accepted Audit Standards. (Dönmez et al., 2005: 58)

This Directive clarified about the terms of auditor's responsibilities, education, requirements of professional expertise and independency in auditing. Even though it did not fully regulate audit standards, it acted advisory for forming of standards in member countries. In the articles of Eight Directive, there are only explanations about general standards but no explanations and comparisons about working field and reporting standards. (Dönmez et al., 2005: 58)

1.3.6 Development of Audit in Japan

In Japan, Independent Public Accountancy Law was established in 1948. American Institute of Accountant Experts has great contributions to legal regulations in this country. (Çarıkçıoğlu, 2006:150)

It is possible to divide the audit performed by public accountants in Japan in two. First, one is audit of financial statements by certified public accountants as required by law. (Legal Audit). The other one is audit of financial statements as a result of companies' own wish. (Solakoğlu, 1991: 65)

In Japan, every joint-stock company has to have one or more auditor elected by general assembly. These auditors before presented to the general assembly audit financial reports. Since it is considered that these auditors would not be efficient enough in protecting the investors because of their dependency to the administration, Capital Market Law obligates the audit of financial reports by Independent and Public Accountants. (Solakoğlu, 1991: 65)

1.4 Relation between Accounting and Auditing

There are important differences between the goals and methods of accounting process in which financial statements depend upon and the goals and methods of audit process in which these statements' reliability were examined. (Güredin, 1997:13)

Accounting is the process of recording, classifying and summarizing economic events in a logical manner for providing financial information for decision makers. The overall objective of accounting is to provide financial information about economic entities that is useful in making economic decisions. (Arens and Loebbecke, 1976: 6)

The primary purpose of auditing is to test assertions (often accounting measurements) and to provide assurance on those assertions. When auditing financial statements the auditor must understand the accounting principles underlying the statements. (Guy et al., 1999: 8)

In addition to understanding accounting principles, the auditor must also possess expertise in the accumulation and interpretation of audit evidence. This major characteristic distinguishes auditors from accountants. (Arens and Loebbecke, 1976: 6)

1.5 Types of Audit

Types of audit can be classified in three main groups:

1. Types of audit according to goals.
2. Types of audit according to auditor's status.
3. Types of audit according to performing reason**.**

1.5.1 Types of Audits According To Goals

There are four types of audit according to goals. That is, audit of financial statements, compliance audit, operational audit and special purpose audit.

1.5.1.1 Audit of Financial Statements

The purpose of financial statement audit is to determine whether the overall financial statements present fairly in accordance with specified criteria. This type of audit usually covers the basic set of financial statements (balance sheet, income statement, statements of stockholders' equity and a statement of cash flows), and generally accepted accounting principles serve as the criteria. (Messier, 1997: 11-12)

In theory and in practice, the most commonly used audit type is the audit of financial statements. Both independent and public auditors performed this audit. In enterprises, by means of auditing financial statements, improper and fraud were detected and in that way financial statement could be presented reliable. (Akgül, 2000: 8)

1.5.1.2 Compliance Audit

The purpose of a compliance audit is to determine whether the auditee is following specific procedures or rules set down by some higher authority. (Arens and Loebbecke, 1976: 7)

In this type of audit, determined criteria were composed by different sources. Initially these are policies, methods and internal control procedures formed by enterprises to provide stability in their own structure. To determine whether the procedures were followed or not compliance audit was realized. (Akgül, 2000: 8)

1.5.1.3 Operational Audit

Audit concerned with the effectiveness and efficiency of the organization are known as operational audit. Effectiveness measures how successfully an organization achieves its goals and objectives. Efficiency measures how well an entity uses its resources to achieve its goals. (Guy et al., 1999:10)

Since the criteria for effectiveness and efficiency were not as clearly stated as the generally accepted accounting principles and as many laws and regulations, an operational audit tends to require more subjective judgment than the audits of financial statements or compliance audits. Mostly, quantifiable criteria must be developed by the auditors to be used to measure the effectiveness or efficiency of the department. (Whittington and Pany, 2001: 11)

1.5.1.4 Special Purpose Audit

Special purpose audit examines the enterprises' financial statements and the documents with the aim of providing detailed information in a specific subject. We can state the following as special purpose audit types: (Aksoy, 2002: 59)

- Research of an exposure corruption and failure
- Special examinations made by courts
- Inspections and examinations made by public institutions
- Inspections and examinations oriented to tax
- Examinations made before loan procedures
- Examinations made before take over, hand over and mergers

In this sort of auditing practices information as a subject for study and the criteria which will be compared by, vary according to the information demanded from auditor. These auditing studies which have a different specific topic, requires auditor who are extremely profound and experienced in relevant topic. (Dönmez, 2002: 9)

1.5.2 Types of Audit According To Auditor's Status

Types of audits according to auditor's status are external audit, internal audit and public audit.

1.5.2.1 External Audit

An external audit is the audit that was performed by an independent person or firm of professional skills. The independent auditor is not an employee of the firm. (Holmes, 1966: 2) Experts conduct this audit in accordance with the requirements, which were defined by or on behalf of the parties for whose benefit the audit is conducted. (Porter et al., 1996: 6)

Independent external audit; comprises financial statement audit, compliance audit and operational audit. (Güredin, 1997: 9)

1.5.2.2 Internal Audit

In contrast to external audit, internal audit is conducted by employees of firm. The internal auditor establishes and appraises financial and operating procedures, reviews financial records and operating procedures, evaluates the system of internal control, periodically summarizes the result of the continuous investigation, prepares recommendations for better procedures, and reports the result to management. (Holmes, 1966: 3)

1.5.2.3. Public Audit

Public auditing expresses financial statement, compliance and operational audits performed by people who are assigned and authorized by laws for the purpose of fulfilling the needs of public. (Akgül, 2000: 11)

1.5.3 Types of Audit According To Performing Reason

There are two types of audit according to performing reason, compulsory audit and optional audit.

1.5.3.1 Compulsory (Legal) Audit

It is the obligatory audit as required by current laws. In this sort of audit, it is manifested by laws and regulations that when and by whom the audit would be performed. (Akgül, 2000: 13)

In some special circumstances, it was observed that legal auditing is performed. In this audit type which is a special way of legal one, public auditors may perform special audit in the occasion of foundation, recapitalization and decapitalization, liquidation, merger of stock companies. (Dönmez, 2002: 11)

1.5.3.2 Optional Audit

Although there is no legal obligation, it is an audit study performed by request of different benefit groups relevant with enterprise. Management determines dimensions and boundaries of this audit. (Akgül, 2002: 13)

1.6 Term of Auditor

Auditor is a specialized person, who performs the auditing activity, possesses adequate professional knowledge and experience, can act independently and has moral qualifications. (Ataman et al., 2001: 21)

We can classify auditors in three main groups:

1. External Auditors
2. Internal Auditors
3. Public Auditors

1.6.1 External Auditors

External auditors were usually referred as independent auditors. External auditors were not employed by the organization being audited. An external auditor conducts financial statement, compliance and operational audits for publicly traded and private companies, partnerships, municipalities, individuals and other types of organizations. (Messier, 1997: 13)

External auditor should observe enterprise activities in an independent way with a systematical examination and a critical aspect. Advise the company to take necessary measurements for enterprise to work more efficient and in accordance with fiscal rules. (Akgül, 2000: 16)

1.6.2 Internal Auditors

Auditors employed by individual companies, partnerships, government agencies; individuals and other entities are called internal auditors. (Messier, 1997: 13) They are mainly concerned with determining whether or not organizational rules and procedures have been followed and the companies' assets were protected. Also, they may be involved with reviewing the effectiveness and efficiency of operating procedures. Internal auditors primarily perform compliance audits and operational audits. (Guy et al., 1999: 13-14)

1.6.3 Public Auditors

Auditors work in public institutions and serving for public benefits, are called public auditor. Bases of public auditors are laws, regulations and general policies. Public auditors perform internal audit in their own institutions and public audit duty in private sector company. (Ataman et al., 2001: 22)

1.7 Independent External Audit

Definition of independent external audit is not very different from the term of auditing. The general definitions of independent external audit are as follows.

Independent external audit; is delivering the results to companies relevant and users, these results are figured out by examining the financial statements impartially, those belong to the audited enterprise, in the aspect of pre-determined principles and rules by an independent auditor following the evidence gathering and evaluating methods and auditing standards. (Beyazıtlı, 1991: 9)

According to an another definition, independent audit: is audit study, for determining the correspondence degree of enterprises financial statement with generally accepted accounting principles, performed by people who are partners of an audit firm or working for their own as self-employers. (Kepekçi, 1998: 7)

Capital Market Board (CMB) defines external audit as "examination of accounts and operations of partnerships and assistance institutions by audit staff authorized by independent auditing institutions according to the auditing principles, basics and standards and depending on the results of this examination detection and reporting of whether these composed financial statements reflect the facts in the framework of Law No: 2499 or not. (Regulation on Independent External Audit in Capital Markets, Article 5)

1.7.1 Goals of Independent External Audit

Main goals of independent external audit are as following; (Aksoy, 2002: 73)

1. Independent audit helps to protect the rights and benefits of people who have debit and credit from the firms.
2. Protect the rights and benefits of business owners, partners or shareholders.
3. Protect the rights and benefits of the audited enterprises.
4. Protect the rights and benefits of the employees of audited enterprises.
5. To provide the development of capital market in state economy and efficient usage of sources supplied by savers to this market.

1.7.2 Benefits of Independent External Audit

Independent audit provides benefit to different social groups and regulates economic life. Benefits of independent audit can be examined in three groups as:

a) Benefits for audited enterprises,

b) Benefits for other members of business life,

c) Benefits for public institutions.

1.7.2.1. Benefits for Audited Enterprises

- Independent audit increases the reliability of financial statements

-Prevent the management and staff to cheat

-Audited financial statements provide the extension of loan opportunities. (Güredin, 1997: 16)

-Independent audit exposes the material errors in account records of audited enterprises and by doing this helps to show the incomes and expenditures properly

-Management becomes stronger and more successful by external audit, which detects the current defects by examining the internal control system. (Aksoy, 2002: 77)

1.7.2.2. Benefits for Other Members of Business Life

-Audited statements help the credit foundations with their decisions about loaning

-Audited statements throw light on investors for their investment decisions

-Audited financial statements provides reliable information to relevant people, especially to the ones having business affair with company, about the profitability, operation productivity, and the financial structure situation of audited enterprise.(Güredin, 1997: 16-17)

-Independently audited financial statements help employers and unions by providing objective information in the negotiations about wages and social supports. (Aksoy, 2002: 79)

1.7.2.3. Benefits for Public Institutions

-It helps to increase the trust to the tax declarations and financial reports prepared on the basis of audited financial statements.

-Independent audit of financial statements belong to the foundations operating for public good, constricts the content of audit of these foundations that would be performed by official institutions

-Independently audited financial statements provide independent and reliable information to the legal authorities for preparing proxy and partnership contracts in case of high debits and bankruptcy. (Güredin, 1997: 16-17)

1.7.3 Limitations of Independent External Audit

There are three types of limitation in independent external audit. These are;

1. Content limitation in independent external audit.
2. Assessment limitation in independent external audit.
3. Comparison limitation in independent external audit.

1.7.3.1 Content Limitation in Independent External Audit

Examination of all records and operations of enterprises is not in question in external audit. External audit is performed by the examination of records and operations chosen according to the importance of topics in audited enterprises and statistical hypothesis. (Aksoy, 2002: 78)

1.7.3.2 Assessment Limitation in Independent External Audit

Independent external audit comprises the examination of accuracy of numeric information. Auditing of management decisions' accuracy and management style is not in question in external audit. External audit generally comprises the assessments made about the coherence of account records and operations with accounting principles and standards and whether prepared in the framework of relevant regulations or not and whether the financial statements reflect the real situation of enterprises or not. (Aksoy, 2002: 78)

1.7.3.3 Comparison Limitation in Independent External Audit

Although profit amount is an indicator that makes the comparison of companies possible, just it is not sufficient. Goal of external audit is making comparisons between companies by determining the accuracy and consistency of financial statements with accounting principles and rules, not reduction of all financial statements in a number and compare with other statements. (Aksoy, 2002: 79)

1.7.4 Factors Limiting Independent External Audit

There are many limitations in audit of financial statements performed according to generally accepted auditing standards. Some of these are:

1.7.4.1 Auditors Study in Restricted Economic Conditions

Audit is useful if performed with appropriate time period and cost. Cost restriction in audit process shows itself in testing of account records and supportive evidences. (Kepekçi, 1998: 13)

1.7.4.2. Time Restriction

Auditor report concerning financial statements is published approximately three months after balance sheet date. This situation may affect the number of evidences related with the events that may affect financial statements and occur after balance sheet date. Moreover, in balance sheet date, time is very limited to wait for the solutions of current ambiguities. (Kepekçi, 1998: 13)

1.7.4.3 Restrictions Originated From Account System

Applying different principles and methods for composing financial statements in generally accepted accounting principles is possible. Recording operation according to the estimations is an inseparable piece of account process. Even though records concerning obscurities are made, no one can predict the results of them. (Kepekçi, 1998: 13)

SECTION II
GENERALLY ACCEPTED AUDITING STANDARDS

2.1 Establishment of Generally Accepted Auditing Standards

Following the audit study, the auditor gives an opinion on the financial tables, and financial table users benefit from this opinion during decision-making process. Therefore, both the auditor must be competent and the audit study conducted must be at a certain quality. This quality and reliability can be maintained by auditing standards (Uğur, 1999: 39). Auditing standards are the general principles that help the auditor fulfill his/her professional responsibilities and enlighten him/her during audit activities.

In order to ensure their impartiality, the auditing standards must be set forth in laws or by the entities of the profession and in practical terms, must be generally accepted. Main standards that are set for external audit of companies and must be observed by the auditor during their works are called "Generally Accepted Auditing Standards". (Aksoy, 2002: 105)

Auditing standards were published for the first time in 1947 by AICPA under the title "Generally Accepted Auditing Standards (GAAS)". Since then, despite the changes in the audit implementation techniques, standards changed a little bit. (Beyazıtlı, 1991: 75) There exists a similarity between the international auditing standards published by International Federation of Accountants (IFAC) and these standards. (Kepekçi, 1998: 14)

Generally Accepted Auditing Standards are the overall guidelines for audit work. These standards establish the framework in which auditor decides necessary action to take in preparing for the examination of financial statements, in performing the examination, and in writing the report. These standards serve to measure the quality of audit objectives and the acts performed to reach these objectives. (Cook and Winkle, 1988: 32-33)

Generally accepted auditing standards are the minimum standards required to be followed during audit activities. These should not be regarded as maximum standards. An auditor who limits the scope of audit only by taking standards as ground without considering the situation faced would be acting against the spirit of auditing standards. Moreover, existence of auditing standards does not imply that the auditor must blindly implement them. In cases where the auditor finds out that guidance provided by the standard cannot be applied to a particular case he/she faced, it will be inevitable for the auditor to decide himself/herself and follow some other path. However, in such a circumstance, all responsibility would rest with the auditor. (Güredin, 1997: 26)

Generally accepted auditing standards are expressed in ten statements divided into three groups: general standards, standards of fieldwork, and standards of reporting. Each standard is discussed individually in the third part of this study.

2.1.1 Historical Development of Generally Accepted Auditing Standards

If we look at the historical background of GAAS, the first development was the formation of the Committee on Auditing Procedure by the AICPA to evaluate, discuss, and issue guidance exclusively on auditing-related matters. This Committee is considered the antecessor of the Auditing Standards Board, and was the first to issue Statements on auditing standards and principles to the public accounting community.

In 1941 Committee issued a pamphlet titled *Statements on Auditing Procedure*, which discussed the auditor's responsibility in applying judgment in audits. It was followed by a series of numbered pronouncements called *Statements on Auditing Procedures*, or SAP. The "Codification of Statements on Auditing Procedure" was issued by the Committee on Auditing Procedure in 1951 to consolidate the features of the first 24 pronouncements which were of continuing usefulness. (Historical Background, AICPA Operating Policies Appendix A; 15-16)

When the Securities and Exchange Commission adopted the requirement that a representation on compliance with generally accepted auditing standards be included in the independent auditor's report on financial statements filed with the Commission, it became apparent that a pronouncement was needed to define these standards. Accordingly, the Committee undertook a special study of auditing standards and submitted a report that was published in October 1947 under the title "Tentative Statement of Auditing Standards—Their Generally Accepted Significance and Scope." The recommendations of this brochure ceased to be tentative when, at the September 1948 meeting, the membership of the AICPS approved the summarized statement of auditing standards. In 1963, the Committee issued *Statement on Auditing Procedure No. 33* to consolidate and replace various pronouncements issued between 1949 and 1963, including pamphlets and statements. (Historical Background, AICPA Operating Policies Appendix A; 15-16)

2.1.2 Statements on Auditing Standards

Auditing standards must have a flexible structure and when necessary, can be easily changed in order to be attuned to fast-changing economic and social conditions. Therefore, standards must be reviewed at certain intervals and necessary adjustments as well as improvements should be made. Otherwise, standards cannot provide expected benefit. (Dönmez, 2002: 57)

In 1972, the AICPA implemented significant changes to its standard-setting practices by consolidating all auditing pronouncements up to that date under Statements on Auditing Standards (SAS), and gave the Committee the title of senior technical committee charged with interpreting generally accepted auditing standards while changing its name to Auditing Standards Executive Committee. From 1972 through 1978 the Executive Committee issued SAS as the authoritative guidelines and rules for auditing, issuing a total of 23 SAS. (Historical Background, AICPA Operating Policies Appendix A; 16-17)

The SASs are considered to be interpretations of the 10 generally accepted auditing standards. They are the most authoritative references that auditor can utilize to resolve problem encountered during an audit. The authoritative status of SASs, as interpretations of ten generally accepted standards, is derived from the AICPA Code of Professional Conduct (Rule202). The Code recognizes the SAS as interpretations of generally accepted auditing standards and requires auditors to adhere to these pronouncements. (Meigs et.al., 1989: 23)

Even though the generally accepted auditing standards and Statements on Auditing Standards are the authoritative guidelines for members of profession, they provide less direction to auditors than might be suspected. There almost no specific audit procedures required by the standards; and there are no specific requirements for determining sample size, selecting sample items from the population for testing or evaluating results. Many practitioners believe the standards should provide more clearly defined guidelines for determining the extent of evidence to be accumulated. On the other hand, highly specific requirements could turn auditing into mechanistic evidence gathering, void of professional judgment. (Arens and Loebbecke, 1976: 40)

Yet, audit is a mental activity and directly grounded on professional judgment. Ruling this out would damage the structure and nature of audit activity. For this reason, it would be more appropriate that audit operations rather be kept inclusive in the form of general code of conducts bestowing freedom of behavior and judgment and required to be observed, than simply being standardized as exhaustive specific rules. (Güredin, 1997: 26)

2.2 Regulatory Institutions That Play Role in Generally Accepted Auditing Standards

American Institute of Certified Public Accountants and Auditing Standards Board are the institutions that play role in the establishment and implementation of Generally Accepted Auditing Standards.

2.2.1 American Institute of Certified Public Accountants

American Institute of Certified Public Accountants is the national professional organization for Certified Public Accountants (CPAs) in the United States of America, with more than 330,000 members, including accountants in business and industry, public practice, government, and education; student affiliates; and international associates. Originally founded in 1887 as the American Association of Public Accountants, the AICPA has had an enormous effect on both accounting and auditing and performs variety of functions, including setting auditing standards, upholding the profession code of conduct, providing continuing education, and preparing and grading the Uniform CPA Examination. (Guy et al., 1999; 14)

The purposes of the AICPA are,

1. To unite the profession of accountancy as constituted by CPAs,
2. To promote and maintain high professional and moral standards within the accountancy profession,
3. To develop and maintain standards for the examination of CPA candidates and
4. To encourage relations among CPAs in America and their equivalents abroad. (Willingham and Carmichael, 1975: 24)

The AICPA sets *generally accepted* professional and technical standards for CPAs in many areas. Until the 1970s, the AICPA held a virtual monopoly in this field. As a result, in 1972 primary responsibility for setting accounting standards was moved from the AICPA to a full-time independent body called the Financial Accounting Standards Board (FASB), which today sets the ground rules for measuring, reporting, and disclosing information in financial statements of non-governmental entities. (http://thecaq.aicpa.org/Resources/Sarbanes+Oxley/Archive+A+Brief+History+of+Self+Regulation.htm)

AICPA members who perform auditing and other related professional services have been required to comply with Statements on Auditing Standards promulgated by the AICPA Auditing Standards Board. In the early 2000s, federal public policy makers concluded that where independent financial statement audits of public companies regulated by the U.S. Securities and Exchange Commission are concerned, that the AICPA's standards setting and related enforcement roles should be transferred to a government empowered body with more enforcement authority than a non-governmental professional association, such as the AICPA could provide. As a result, the Sarbanes-Oxley law created the Public Company Accounting Oversight

Board (PCAOB) which has authority to promulgate auditing and related attestation standards, quality control, ethics, independence and other standards relating to the preparation and issuance of audit reports for issuers.

However, the AICPA retains its considerable standards setting, ethics enforcement and firm practice quality monitoring roles for the majority of practicing CPAs, who serve privately held business and individuals. (Changes created by Sarbanes Oxley Act of 2002, AICPA Operating Policies; 17-18)

Rules and Standards issued by the AICPA are;

- Bylaws
- Code of Professional Conduct
- Statements on Auditing Standards
- Statements on Standards for Accounting and Review Services
- Statements on Standards for Attestation Engagements
- Statements on Quality Control Standards
- Standards for Performing and Reporting on Peer Reviews
- Statements on Standards for Consulting Services
- Statements on Responsibilities in Tax Practice (Messeir, 1997:24

2.2.2 Auditing Standard Board

Auditing Standard Board (ASB) was formed as the successor to prior senior technical committees on auditing matters in October 1978 by AICPA. The ASB is responsible for the promulgation of auditing and attestation standards and procedures to be observed by members of the AICPA in accordance with the AICPA's Bylaws and *Code of Professional Conduct*. (AICPA Operating Policies; 1)

The mission of the ASB is to develop and communicate comprehensive performance, reporting, and quality control standards and practice guidance to enable auditors of non-issuers to provide high quality, objective audit and attestation services at a reasonable cost and in the best interests of the profession and the beneficiaries of those services, with the ultimate purpose of serving the public interest by improving existing and enabling new audit and attestation services. The ASB accomplishes this mission by (1) developing auditing, attestation, and quality control standards that inspire public trust, (2) contributing to the development of high quality international auditing and assurance standards, and (3) responding timely to the need for guidance and communicating it clearly to the profession and to users. (AICPA Operating Policies; 2)

The Sarbanes-Oxley Act of 2002 changed the hierarchy of generally accepted auditing principles and standards. The legislation established that the new PCAOB and the Securities Exchange Commission (SEC) now had final authority over auditing regulation and public-auditor professional-practices standards for audits of public companies, also referred to as "issuers". Public accountants and firms who audit public companies were required to register with the PCAOB and follow all standards, principles, rules, and interpretations issued by the PCAOB in regard to public company audits and audit reports, as well as attestation and quality control. The PCAOB adopted the ASB's auditing and attest standards as its temporary auditing rules in 2003. (Changes created by Sarbanes Oxley Act of 2002, AICPA Operating Policies; 17-18)

The AICPA subsequently changed the designation of the leading GAAS-setting authority in February 2004. It designated the PCAOB as the authoritative body for GAAS related to public companies, while the ASB was designated for non-public companies. (Changes created by Sarbanes Oxley Act of 2002, AICPA Operating Policies; 18)

2.3 Development of Independent External Audit in Turkey

From the 1970's, increase of international relations of enterprises in our country increased the investments of foreign enterprises. Enterprises were forced to work with foreign credit institutions, because they went through a bad patch due to economic conditions. These credit institutions' demand applying enterprises' financial statements being audited let the audit emerge as an obliged necessity and pioneered the development of it in Turkey. (Havan, 2006: 54)

Until 1987 audit of financial statements were performed in the framework of Turkish Commercial Code and tax legislation in Turkey. In the historical flow audit term first showed itself in Turkish Commercial Code in Turkey. (Beyazıtlı, 1991: 64)

Obligation of independent external audit first came in to agenda in 1987 with the auditing of banks in Turkey. With these developments, Central Bank of Republic of Turkey published Regulation about Independent Auditing, which explains the basis of bank audits by independent audit institutions. (Akgül, 2000: 5).

After the auditing of banks, audit of co-operations, which were subject to CMB, became obligatory. Capital Market Board published Regulation about Independent External Audit in Capital Markets in 13 December 1987 to regulate the audit of partnerships and supporter institutions. Independent Audit Institutions are established due to this regulation. Capital Market Board with the communiqué determined the general basis, auditing standards, reporting principles and rules concerning auditing institutions and auditors.

Capital Market Board published Serial's No: 19 Communiqué in 02.11.2002 to provide auditor independency in the parallel of Sarbanes-Oxley Act, which was put in force to prevent the auditing scandals experienced nowadays. With this communiqué, some articles added to Communiqué Serial's No: 16 and some articles were changed. (Dönmez et al., 2005: 58)

In our country one of the most important development in audit is publication of the Certified Public Accountancy and Sworn in Certified Public Accountancy Law No: 3568 in 13 June 1989 and the publication of related regulations and communiqués. (Akgül, 2000:5)

2.3.1 Independent External Auditing Within the Capital Market Legislation

In our country independent external audit applications started with Capital Market Law No: 2499. In the 16th article of law, obligation of independent auditing of financial statements composed by the institutions subject to this law, basis of special auditing, juristic responsibilities of auditing institutions and announcement of audit reports are regulated. (Küçüksözen ve Sayar, 2002: 50-51) According to article 16;

"Issuers and capital market institutions shall prepare financial statements, financial reports and other information required by the Board to be disclosed, including consolidated financial statements, in compliance with the form and principles to be determined and generally accepted accounting principles, definitions and standards.

Issuers and capital market institutions shall have the financial statements, which are identified by the Board audited by independent auditing firms previously established and to be established according to paragraph (d) of Article 22, with respect to the compliance with the principle of fair presentation of the accuracy and reality of information.

The Board may require independent auditing reports in connection with public offerings, at the phase of adopting the registered capital system, and in the cases of liquidation, transfer, merger or status changes of joint stock corporations and capital market institutions that are subject to this Law.

Independent auditing firms are legally responsible for losses arising from false or misleading information and statements in the auditing reports they have prepared for the financial statements and reports that they have audited.

Financial statements and reports required by the Board, and, in the case of financial statements subject to independent audit, the reports of the independent auditors, shall be provided to the Board and disclosed in accordance with the principles and procedure established by the Board."

Another arrangement about independent external audit is in 22nd Article of Capital Market Law. In 22/d;

"To determine the principles related to independent auditing operations, including when appropriate with respect to use of electronic media in the capital markets; to determine the conditions for establishment and the working principles of institutions engaged in independent auditing operations with respect to the capital market according to Law No. 3568, dated 1 June 1989 by consulting with the Union of Chambers of Public Accountants of Turkey and to publish lists of those who have such qualifications."

Capital Market Board realized the main layout with Regulation on Independent External Audit published at Official Gazette in 13.12.1987 with number 19663 and Communiqué About Independent External Audit In Capital Markets (Serial: X No:16) published at Official Gazette in 04.03.1996 with number 22570.

The other communiqués issued by CMB regarding to independent external audit are following;

- Communiqué About Determination Of Corporations Subject To Special Auditing (Serial: X No:7)
- Communiqué About Determination Of Corporations and Institutions Subject To Perpetual And Limited Auditing (Serial: X No:12)
- Communiqué About Announcement Of Independent External Audit Institutions To Public (Serial: X No:15)
- Communiqué on the Independent Audit Standards In Capital Markets (Serial: X No: 22)

Communiqués mentioned above were abolished by Communiqué on the Independent Audit Standards in Capital Markets issued in Official Gazette in 12.06.2006 with number 26196. With this Communiqué; standards, principles, methods and basis' about independent external audit, independent audit institutions and independent auditors were gathered in one hand.

In the 4th Article of Communiqué on the Independent Audit Standards In Capital Markets, independent audit is described as: "auditing and reporting of all records and documents by using all necessary independent audit techniques required in auditing standards for obtaining reasonably ensuring and appropriate independent audit evidences regarding to the integrity and suitability of annual financial statements and other financial information those would be announced to public or may be demanded by Board, with financial reporting standards.

In the 3rd Article of mentioned Communiqué goal of independent audit of financial statements is explained as; making independent auditors to deliver opinion about whether financial statements reflects the situation of enterprise suitably and truly through the financial reporting standards or not.

The enterprises, which annual financial statements those would be announced to public or may be demanded by Board are subject to independent auditing, are following (Serial: X No:22; Article 3) :

- Joint-stock companies whom shares are processed in securities exchange and/or in organized other markets
- Corporations whom shares are offered to public or considered so.
- Banks only for brokering activities
- Stock brokers
- Portfolio management companies
- Investment Funds
- Retirement investment funds
- Mutual Funds
- Housing Finance Funds

- Asset Finance Funds
- Mortgage Finance Funds
- Stock markets, other organized markets, barter and custody institutions regulated in Law and working as share companies.
- Enterprises whom financial statements' auditing is required by Board

Board stipulates the external audit be performed by auditing institutions having certain qualifications. Qualifications required by Board are following (Serial: X No:22; Article 3):

a) To be founded as share company and shares to be registered.

b) Trade name including "independent audit" expression

c) Shareholders to be real person having the qualifications indicated at the Article with the title "Executives and Independent Auditors" (stipulations at the (ç), (d), (h) of 1 st paragraph of mentioned Article are not required for all shareholders. Furthermore this stipulation is not required in case of an abroad centered institution joining to an independent audit institution in our country with the same working methods.

ç) Responsible partner chief auditors to have minimum the % 51 of registered capital.

d) Operate only in independent audit and profession field.

e) Organization, residence, technical equipment, order of document and register to be sufficient for carrying out the independent audit business.

f) To have Professional Responsibility Insurance in the framework of basis determined The Undersecretariat Of Treasury or The Ministry it is bound to.

- Executives and auditors of independent audit institutions should have the qualifications given below to be given the authority of independent auditing by Capital Market Board. (Serial: X No: 22; Article 4)

- To have the title of Certified Public Accountancy and Sworn-In Certified Public Accountancy in accordance with Law No: 3568 or to have a certificate which provides auditing authority in foreign countries.
- Not to be bankrupt or sentenced for a disgraceful crime
- To be resident in Turkey
- Responsible partners chief auditors to have worked at least two years in independent auditing institutions those are at the list of Board as auditor, senior auditor or chief auditor, for independent auditing of capital market institutions and joint-stock companies which are open to public or to have worked as Board Member for two years or Board Staff for five years.
- To have Certificate Of Independent Audit In Capital Markets
- Not to be banned permanently because of their responsibility for independent audit activities performed in institutions that independent audit authority is cancelled due to these activities or if banned permanently to be re-given the authority by Board at the end of penalty time.
- Not to be one of people who have responsibility for cancellation, in the enterprises that operation authority license (s) or stock membership are cancelled.
- Inexistence of verdict of conviction due to opposition to the Law.
- Not to be banned from operating in capital markets due to the relevant articles of Law.
- Full-time duty in independent audit institution.

2.3.2 Independent External Auditing Within the Certified Public Accountancy and Sworn In Certified Public Accountancy Legislation

With the Law of Certified Public Accountancy and Sworn-In Certified Public Accountancy issued in Official Gazette in 13.06.1989 with number 20194 accounting profession gained legal ground. The objectives of this Law; "are to ensure the healthy and reliable functioning of operations and transactions in enterprises to audit and evaluate the results of the operations within the framework of the relevant legislation, to present the actual facts to the use of the concerned persons and authorities, to regulate the fundamentals concerning the establishment, organization, operations, activities and the elections of the principle organs of "Certified Public Accountancy" and "Sworn-in Certified Public Accountancy " and the Chambers of Certified Public Accountants and Sworn in Certified Public Accountants." (Law of Certified Public Accountancy and Sworn-In Certified Public Accountancy; Article 1)

With this law accountancy profession is divided in two main groups as performers and auditors. The ones performing accountancy profession are titled as Certified Public Accountant, and the ones performing auditing are titled as Sworn-in Certified Public Accountant.

The subjects of the profession of Certified Public Accountancy comprise the following services rendered to enterprises and business concerns owned by real and legal persons.

- To keep books, prepare the balance sheets, profit and loss statements, tax returns and other relevant documents in compliance with generally accepted accounting principles and the provisions of the relevant legislation.
- To establish and improve accounting systems: to regulate administration, accounting, finance, financial legislation, to perform the jobs related to their applications, and to provide advisory services in the related fields.
- Based on the relevant documents on issues specified in the a fore mentioned paragraph, to perform investigations, analyses and audit, to present written opinions regarding financial statements and tax returns, to prepare reports and similar documents, to perform arbitration, expertise and similar services.

Persons, who perform the activities mentioned above independent from a business entity, are defined as Certified Public Accountants.

In addition to the duties of Certified Public Accountant, subject of the profession of Sworn-in Certified Public Accountancy also includes the application of certification within the framework of the regulation to be promulgated in compliance with Article 12 of the Law.

Beside this, some prohibitions are brought for Sworn-in Certified Public Accountancy. Sworn-in Certified Public Accountants cannot keep books related to accounting, cannot establish an accounting office and cannot become partners to the accounting offices already established.

Regulation About The Working Methods and Basis Of Certified Public Accountants and Sworn-in Certified Public Accountants was issued in 03.01.1990, for the purpose of determining the methods and basis concerning the auditing study that Certified Public Accountants and Sworn-in Certified Public Accountants would perform.

In the 48th Article of Regulation, accountancy and auditing terms are defined as:

Accountancy; regulates the computational records of economic activities of foundations and institutions, delivers this information truly and clearly to the relevant with activities and results.

Auditing; is a systematic study which impartially researches and approves by evidences whether the real nature of economic activities take place in records or not in accordance with relevant legislation and generally accepted accounting principles.

According to the 49th Article of the same Regulation, goal of audit is expressed as " to prove that the records in financial statements of firms, foundations and institutions are realistic, truthful and reliable to their owner and partners, creditors and credit institutions, employee and employer institutions, economic and administrative units of government and tax administration."

Certified Public Accountants and Sworn-in Certified Public Accountants determine whether the information provided to relevant by foundations and institutions are realistic, truthful and reliable by performing the auditing activities mentioned below (Regulation About The Working Methods and Basis Of Certified Public Accountants and Sworn-in Certified Public Accountants; Article 50):

a) Whether the assets of foundations and institutions are used for benefits of themselves or not.

b) Whether the item and value of assets are shown in records or not.

c) Whether the assets are valued suitably and truly in accordance with relevant legislation and account principles or not.

d) Whether incoming and outgoing values are recorded exactly and accurately or not.

e) Whether the increases and decreases of debts and receivables of enterprise are shown exactly and accurately or not

f) Whether the increases and decreases of assets by the economic activities of foundations and institutions are calculated exactly and accurately in records and financial statements or not

g) Whether the financial statements are composed suitably with relevant legislation and generally accepted account principles or not

h) Whether tax declarations, other declarations and documents are convenient with relevant legislation or not

In the 12th Article of mentioned Law certification duty of Sworn-in Certified Public Accountants and their responsibility arise from certification are regulated. According to this,

"Sworn-in Certified Public Accountants certify the compliance of the financial statements and tax returns prepared by individuals and entities and the enterprises and establishments thereof, with the provisions specified in the legislations, accounting principles and the accounting standards, and further certify that the accounts have been inspected in accordance with the auditing standards.

Certified financial statements submitted to public institutions and establishments pursuant to the laws, are considered as documents investigated within the framework of the certification, by the officials of the relevant public institution or establishment. However, issues related to the exercise of authorities of inspection and investigation granted to public administration through various laws and the recurrence of such authorizations when deemed necessary, remains reserved.

Sworn-in Certified Public Accountants are responsible from the verifiability of the certification. If a defect occurs in the verifiability of the certification, the concerned sworn-in Certified Public Accountants shall be held responsible jointly and successively with the liable taxpayer in the penalties and the tax losses, confined to the content of the certification. Sworn-in Certified Public Accountants clearly specify the content of the certification in their reports.

The responsibilities of the performers of the profession in compliance with the provisions of this Law as regards to the tax laws and other legislations are reserved."

Certification duty of SCPA's is laid out with a regulation issued by Finance Ministry besides Law. Regulation about Documents Certified by SCPA's, Certification Subjects, Methods and Basis Concerning Certification was issued in Official Gazette in 02.01.1990 with number 20390.

Goal of certification according to this regulation is;

a) To provide the accurately and realistically compose of financial statements those show the results of account and records of real and legal persons or their firms and enterprises and serve them to the utilization of public.

b) To provide the speed in meeting demands of real and legal persons or their firms and enterprises in the aspect of relevant legislation and to protect their rights and benefits.

c) To make the trust rule in affairs between tax administration and tax payers.(Regulation About Documents Certified by SCPA's, Certification Subjects, Methods and Basis Concerning Certification Article 5)

In the 7th Article of Regulation, issues and documents those can be certified by SCPA's concerning tax legislation are explained. In this article certification issues regarding incentives, reductions, exemptions and immunities which take place in Income Tax, Corporation Tax, Value Added Tax, Inheritance Tax, Law about Collection Methods of Public Credits, Stamp Tax and Fiscal Legislation are mentioned.

2.3.3 Independent External Auditing Within the Banking Legislation

Banks and Special Finance Institutions are among the most important institutions of money and capital markets. Because they accept deposits and perform main functions in economy, they are subject to quite different and heavy auditing and custody than other companies. In this scope, these institutions' financial statements are also subject to independent external audit.

13/1-a Article of Banks Law No: 4389 gives to Banking Regulation and Supervision Agency (BRSA) the authority of making arrangements concerning accounting and recording order of banks. In the 13/2 Article of the same law, BRSA is authorized to lay down provisions applicable to foundation of independent audit firms sand suspension of their operations provisionally and permanently. Depending on this authorization, BRSA issued Regulation Concerning Independent Audit Principles and Regulation about Authorizing Independent Audit Institutions and Abolishing Their Authorization Permanently or Temporarily in Official Journal No: 24657 with the date of January 13 2002. (Başpınar, 2005: 52)

The regulations told above were abolished by Regulation on Authorization and Activities of Institutions to Perform External Audit In Banks which was issued in Official Journey No: 26196 with the date of November 01 2006.

In 5th Article of the mentioned Regulation external audit is defined "as the process consisting of the stages of examining the correctness, reliability, and degree of compliance with the banking regulations, system of accounts and records and financial statements of banks, and collecting evidences to notify the results thereof to the parties concerned, and forming an opinion on and reporting the result of evaluation of such evidences".

According to Regulation three types of independent audit practice is carried out in banks. These are; annual audit, interim audit and special purpose audit.

a) **Annual audit** is the external audit conducted as of the ends of the accounting period in a fully comprehensive manner and by using all audit techniques required.

b) **Interim audit** is the external audit conducted as of interim periods, in line with the annual audit plan, by an authorized audit institution realizing annual audit in accordance the principles and rules of limited audit.

c) **Special-purpose audit** is the external audit conducted under the principles and procedures stated in this Regulation exclusively for the matters, with the exclusion of tax legislation, foreseen in the regulations put into force pursuant to the Law or which are of such special nature as will be determined by the Agency.

Same Article states that external audit activities are practiced having considered the Law and regulations on the Law, other related regulations and international audit standards.

In the 6th Article of Regulation, by whom independent audit activities would be performed, is determined. According to this;

"External audit activities are executed by the external auditors authorized to conduct audit according to the Law Nr. 3568, employed by an authorized audit institution with which the bank concerned has signed an external audit contract, headed by the responsible partner senior auditor concerned of the same authorized audit institution."

In the 15th Article, stipulations required for the partners and auditors of institution, which would perform audit, are stated.

1) Have obtained the power to audit pursuant to the provisions of the Law Nr. 3568, must have the title of sworn-in certified public accountant or certified public consultant registered to relevant professional chamber, or must hold a certificate granting the power to conduct external audit in foreign countries in line with the principles of reciprocity stated in article 8 of the Law Nr. 3568 or other provisions,

2) Not have a partner and must not be chairman or member of board of directors, auditor, manager in another external audit, rating or valuation institution, or must not be employed as a personnel engaged in external audit, rating or valuation activity,

3) Have the qualifications stated in Article 8 (d) of the Law,

4) Not have been found responsible for the activities causing revocation of power in institutions of which authority to conduct external audit, rating or valuation at home or abroad,

5) Must have no commercial activities other than their professional activities,

6) Not have been subjected to a penalty of such nature as to prevent them from engaging in external audit as a result of a disciplinary investigation carried out about themselves by other authorized institutions,

Institutions, which will be authorized to make an audit in banks, must fulfill the following conditions;

1) Must be established as a joint stock company and all of their share certificates must be registered in the name of the holder,

2) Must have the inscriptions: Sworn-in Certified Financial Consultant or Certified Public Accountant in their trade names,

3) Their articles of incorporation must not contain provisions running counter to relevant legislation and the Law Nr. 3568 and the legislation issued on the basis of the said Law,

4) Must have obtained the chamber certificate of activity documenting that they are registered to the related professional chamber established according to the Law Nr. 3568, and an audit company registration certificate from TÜRMOB,

5) Must have a management structure capable of realizing external audit hereunder and sufficient number of external auditors with sufficient qualifications, the required technical equipment, document and record system, and forming the structure and written policies related with quality assurance system,

6) Undertake to take out professional liability insurance in order to meet the losses that may arise from the services they render,

7) Their power to conduct external audit must not have been revoked at home or abroad,

8) Minimum fifty-one percent of their principle capital must belong to responsible partner senior auditors,

9) Undertake to resign from external audit service given to the bank in case of confusion of independence of partners, chairman and members of the board

of directors, managers and auditors disappeared during external audit activity. (Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks; article 14)

2.4 Development of Auditing Standards in Turkey

First auditing standards study in Turkey was setting up of the Unified Accounting System by Reformation Committee between 1964 and 1968; and as of 1972, this system was started to be implemented at state economic enterprises. Thereafter, Capital Markets Board conducted extensive application-oriented studies on auditing standards. (Aksoy, 2002: 107)

In Turkey, auditing principles and rules first gained legal ground with the Communiqués published by Capital Markets Board in 1988. These rules were adopted with a view to ensuring validity of audit carried out at entities subject to the legislation of Capital Markets Board with respect to the capital markets legislation. In the legislation of Capital Markets Board, the principles and rules regarding independent audit are provided for in the Communiqué Serial X No: 16. (Küçüksözen and Sayar, 2002: 51) However, the Capital Markets Board abated the Communiqué Serial X, No: 16 so as to ensure harmonization with "International Auditing Standards" and issued the "Communiqué on Independent Auditing Standards in Capital Market" Serial X, No:22.

Accounting and audit operations in Turkey are carried out as per the Law No: 3568, which regulates the law of accounting profession. Certain provisions of the Regulation on Documents Certified by SCPA, Certification Subjects, Methods and Basis Concerning Certification dated 02.01.1990 and of the Regulation on the Working Methods and Basis of Certified Public Accountants and Sworn-in Certified Public Accountants dated 03.02.1990 enacted based on the Law No: 3568 are in the nature of auditing standard. (Türker and Pekdemir, 2002: 8)

These provisions stipulated under such titles as "general professional standards, procedures and principles of application, work subjects, integrity, impartiality, secrecy, accountability, independency, unfair competition, types of audit reports" have a scope close to both American Auditing Standards and International Auditing and Assurance Standards. (Türker, 2006: 93)

As for banking legislation, the framework of independent audit is regulated in line with international auditing standards in the arrangements with respect to independent audit. (Türker, 2006: 93) With the aim of establishing standards for independent audit in the banking sector, Banking Regulation and Supervision Agency published "the Regulation on Authorization, Revoking Temporarily or Permanently the Authorization of Organizations to Perform Independent Audit" and "the Regulation on Independent Audit Principles". Moreover, the Regulation on the Authorization ad Activities of Organizations to Perform Independent Audit of Banks was published in the Official Journal No: 26333 dated 1 November 2006.

It is seen that the standards in these arrangements are not at the level of generally accepted auditing standards. Hence, the Union of Chambers of Certified Public Accountants of Turkey (TÜRMOB) initiated the studies towards establishment of independent auditing standards that comply with generally accepted auditing standards. This responsibility was later delegated by TÜRMOB to Turkish Accounting and Auditing Standards Board (TMUDESK) founded on the date of February 9, 1994. (Dönmez and Ersoy, 2006: 74)

With the amendment made to Article 27 of the Law No: 4487 and dated 18.12.1999, TMUDESK's duty to establish these standards was transferred to newly established Turkish Accounting Standards Board. The Turkish Accounting and Auditing Standards Board has not published any standard in the area of audit, although it has made progress to a certain extent in the issuing of accounting standards. (Sevim et al., 2006: 8)

One of the most significant developments in Turkey in the area of audit is the establishment of Turkish Auditing Standards Board (TÜDESK) on the date of January 22, 2003. The Law No: 3568 entitles TÜRMOB to establish, with a democratic approach and without being under any supervision, the auditing standards to be implemented in Turkey by the members of accountancy profession in the audit of their works. TÜRMOB has set a framework, though limited, with its Regulation on the Working Methods and Basis of Certified Public Accountants and Sworn-in Certified Public Accountants that has been in force since its inception. Said Regulation includes generally accepted auditing standards on a limited scale. (Türker, 2006: 94)

In Turkey, organizations such as CMB, BRSB, TÜRMOB and the Undersecretariat of Treasury have made separate arrangements that regulate establishment, authorization ad activities of institutions and organizations operating under their authority and responsibility area as well as standards of profession and ethics these institutions and organizations must observe. The fact that there are different arrangements and standards established by different entities leads to contradictions in practical terms. (Uyar and Çelik, 2007: 8)

For this reason, "Draft Law on Turkish Auditing Standards and Public Oversight Agency" developed by the Ministry of Finance was submitted to the Presidency of Turkish Grand National Assembly on 25.06.2008. The purpose in drafting this law is to designate auditing standards by unique authority through eradicating scattered structure in Turkey in the area of independent audit on one hand. On the other hand, it is aimed to establish "Turkish Auditing Standards and Public Oversight Agency" in the nature of a public entity that posses administrative and financial independence with a view to building up a public oversight system. (www.tbmm.gov.tr/komisyon/abuyum/belge/faaliyet/donem23/1-619.pdf) However, The Law on Turkish Auditing Standards and Public Oversight Agency is still a draft and has not been enacted yet.

2.4.1 Regulatory Institutions That Play Role in Auditing Standards in Turkey

In Turkey, mainly three regulatory institutions play role in auditing standards. These are The Union of Certified Public Accountants and Sworn-in Certified Public

Accountants of Turkey, Turkish Accounting and Auditing Standards Board and Turkish Auditing Standards Board.

2.4.1.1 The Union of Certified Public Accountants and Sworn-in Certified Public Accountants of Turkey

The Union of Certified Public Accountants and Sworn-in Certified Public Accountants of Turkey is founded by the Law No. 3568 enacted in 1989 as an official association of the profession through the participation of all the Chambers of Independent Accountants, Certified Public Accountants and Sworn-in Certified Public Accountants. The Union is the unique authority that is empowered to award professional licenses. The Law specifies the qualifications that are required to be possessed to be a member of the profession and only those who have been awarded a license by TÜRMOB are entitled to render professional services. TÜRMOB has four organs, general board, board of directors, board of discipline and board of auditing. (www.turmob.org.tr/TurmobWeb/turkce/english.aspx)

The Union renders a public service and is founded primarily to carry out activities to insure the development of the profession and the protection of the due interests of the members of profession and the preservation of the professional dignity, ethics, order and traditions. In order to fulfill its duties like the development of the profession, protection of the interests of the members and the preservation of the professional ethics and order, the Union extends comprehensive efforts in areas such as awarding of licenses, practical training, examinations, Standard setting, quality control, application and enforcement of professional standards, professional rules and regulations and publications and continuous professional education. (www.turmob.org.tr/TurmobWeb/turkce/english.aspx)

2.4.1.2 Turkish Accounting and Auditing Standards Board

Turkish Accounting and Auditing Standards Board has been founded by TÜRMOB in 1994. The raison de’etre of TMUDESK is to determine and issue the national auditing standards for the members of accounting profession to carry out audit activities in a disciplined manner thanks to the national accounting standards that are to be implemented for public benefit. By doing so, the national accounting principles shall be improved and adopted in a manner to ensure that financial tables audited are appropriate, realistic, reliable, balanced, comparable and understandable.

TMUDESK has so far issued 19 accounting standards. However, since these standards issued by TMUDESK are not within the scope of any arrangement, they do not have sanction power. These standards are just rules recommended in order to guide accounting practices and to ensure compliance with international accountancy. (Başpınar, 2005: 43)

2.4.1.3 Turkish Auditing Standards Board

Turkish Auditing Standards Board was founded with the decision dated February 22, 2003 of TÜRMOB executive board. The objective of TÜDESK is to set and issue national auditing standards for disciplined and regular execution of audit activities performed by professional members certified as per the Law No: 3568 and of audit works required by other laws. In this context, TÜDESK translated into Turkish and issued "International Auditing Standards" to establish national auditing standards in Turkey. Nevertheless, implementation of these standards has delayed due to lack of legal obligation.

The functions of Turkish Auditing Standards Board are as follow:

a) Drawing the "Conceptual Framework" that includes purpose and concepts adopted in specification of national auditing standards as well as Generally Accepted Auditing Standards to be used as basis in setting up of Auditing Standards of Turkey;

b) Establishing national auditing standards in order to report accurate, consistent and comparable accounting information;

c) Keeping auditing standards up-to-date in order to meet changing and emerging requirements;

d) Ensuring consistency of national auditing standards with Internationally Accepted Auditing Standards in order to provide fair, reliable and comparable financial reports in the international arena as well;

e) In due process of forming national auditing standards, asking opinions of professional chambers, audit certified public entities, members of the profession, academicians and similar groups in order to resolve issues faced in practice;

f) Publishing, where necessary, statements for clarification on uncertain issues in the application of national auditing standards;

g) Encouraging recognition by academic environment and use of issued auditing standards in surveys and education, which is directed towards adoption of national auditing standards and raising public awareness for their implementation" (Bilgin, 2006; 17-18)

As is mentioned before, the quality of the audit work is measured with GAASs, which are adopted at international level. These standards are the minimum standards that must be observed during audit study. In this context, third part of the study surveys to what extent the arrangements in Turkey concerning independent external audit within the scope of the legislations on capital market, certified public accountant and sworn-in certified public accountants and banking comply with GAAS.

SECTION III

THE COMPARISON OF INDEPENDENT EXTERNAL AUDIT PERFORMED IN TURKEY WITH GENERALLY ACCEPTED AUDITING STANDARDS

3.1 Purpose of the Study

Independent external audit practices in Turkey are carried out within the framework of capital market, certified public accountancy and sworn-in certified public accountancy and banking legislations. Each one stipulates differing arrangements with respect to independent audit. However, if the audit studies done according to mentioned legislations are to be trusted, they must be performed in line with certain standards. In this respect, GAASs constitute the minimum conditions in guaranteeing the quality of audit. The aim of this study is to detect to what extent the independent external audit currently performed within the scope of these legislations are consistent with GAASs, whereby we shall have an idea on the quality of independent audit works in Turkey.

3.2 Methodology and Limitations of the Study

This study is a qualitative comparative study. In this part, each GAASs are analyzed under two separate titles. The first part dwells on the characteristics of the standard; what follows in the second part is the arrangements regarding the standards in the capital market, certified public accountancy and sworn-in certified public accountancy and banking legislations respectively, a comparison of these arrangements with standards and finally the level of compliance to each standard.

In this study, to what extent the independent external audit practices in Turkey comply with GAASs was measured through analyzing the arrangements made within the framework of mentioned three legislations. Despite the fact that sometimes, the arrangements in the legislations are consistent with GAASs, the situation in practice might be different. Yet, this study assesses independent external audit solely in terms of legislations. Therefore, it might be lacking in determining differences in practical terms.

3.3 General Standards

The general standards concern the qualifications of the auditor and quality of his work. They not only govern auditor's competence, independency and due care, but also effect auditor's fieldwork and reporting. These general standards are also known as personal standards. (Willingham and Carmichael, 1975: 41)

Main hypotheses that general standards are based on and the validity of which have been accepted undisputedly for years are as follows: (Kavut, 2000: 13-14)

a) There is always conflict of interest between the auditor and the management of audited enterprise.

b) If the financial data are examined to give an independent audit opinion, the auditor should behave within the sense of acting independently, which is specific to auditorship profession.

c) Independent auditor is equally responsible vis-à-vis the parties who are directly and indirectly interested in the results of audit. In other words, the auditor has professional responsibilities and obligations against both the managers of audited company and the relevant external parties.

A large part of financial statement users does not know the auditor who gave opinion concerning these statements. Nevertheless, the information users who know that the auditor has the qualifications stated in generally accepted auditing standards and worked in accordance with these standards rely on the opinion given by him/her. (Kepekçi, 1998: 15)

General standards include standards of technical training and proficiency, independence and due professional care.

1. The audit is to be performed by a person or persons having *adequate technical training and proficiency* as an auditor.

2. In all maters relating to the assignment, *independence in mental attitude* is to be maintained by the auditor or auditors.

3. *Due professional care* is to be exercised in the planning and performance of the audit and the preparation of the report. (Meigs et.al., 1989: 20)

3.3.1 Standard of Technical Training and Proficiency

This standard is normally interpreted as requiring the auditor to have formal education in auditing and accounting, adequate practical experience for the work being performed, and to continue professional education. Moreover, auditor must be technically qualified and experienced in those industries in which his audit clients are engaged. (Alvin and Arens; 1976; 39)

An auditor's advanced formal education should not be only in accounting subjects. Rather, auditors should get enough general education to enable to function as a contributing member of society. Successful auditors need the ability to get along with clients and co- workers, both superior and subordinates. Communication talents need to be singled out as being of higher importance to auditors. Even though much accounting information is expressed in figures, they are nearly meaningless if not delivered to users in clearly understandable written or spoken language. (Cook and Winkle, 1988: 36)

Successful auditors realize that technical training received a few years in the past is probably inadequate to satisfy this standard. Auditors have to update their technical training. (Cook and Winkle, 1988: 36) For this reason, auditors should follow the legislation about accounting, auditing and tax, read the professional publication and attend the courses and symposiums. (Kepekçi, 1998: 15)

Much knowledge of auditing can be obtained through college courses, staff training programs, and even self -study. However, some aspect of proficiency can be acquired only through auditing experience. A junior auditor learns by reviewing instructions from experienced auditors and by following examples of their work, also benefits from comments made by supervisors reviewing work in progress and work completed. Even though each audit engagement is different, an auditor should be able to apply auditing skills learned on other engagements by making necessary modifications as dictated by professional judgment. (Cook and Winkle, 1988: 37)

3.3.1.1 Comparison of the Independent External Audit within Turkey with the GAAS

In Turkey, conditions concerning the professional education and proficiency an auditor is expected to have are regulated in the legislations of certified public accountancy and sworn in certified public accountancy, capital market and of Banking.

Arrangements with respect to this standard in the legislation of Capital Markets Board are presented in the Articles 7, 8 and 9 of 2nd part of the Communiqué on the Independent Audit Standards in Capital Markets. (Serial: X No: 22)

In 7 Article of mentioned Communiqué's 2nd part under the title of "*Professional Proficiency*", it is stated that *independent audit institutions should seek for and provide the professional proficiency to their auditors. Professional proficiency is defined as the pre- and post-graduate education as well as professional experience being at a level sufficient to be able to perform independent audit.*

As in the case of technical training and proficiency standard, the Capital Markets Board Communiqué requires the auditor to have at least a degree in higher education so as to perform independent audit. Therefore, we can say that CMB regulations are in parallel with mentioned standard.

Article 8 of the Communiqué regulates the duties entrusted to independent audit institutions, independent auditors and independent assistant auditors with a view to providing and developing professional proficiency. In the process of employing independent assistant auditors, independent audit institutions have to check if they have a degree in higher education and take measures maintaining them to have professional training and to gain experience. Furthermore, they have to determine the existence of professional proficiency by referring to such documents as interview results, official reports of course assessments and the results of examinations held by independent audit institutions or relevant professional associations.

Independent auditors are held responsible for ensuring, maintaining and improving professional proficiency of themselves and of auditors and assistant auditors working with them. For this purpose, independent auditors at all levels have to keep abreast of the legislation related to auditing profession, national and international developments and publications, courses, symposiums and conferences.

As is mentioned above, technical training is not sufficient to satisfy this standard. Auditors should update their technical training by following relevant legislation, reading professional publications and by attending to courses and symposiums related to auditing. Article 8 of the Communiqué stresses as well those independent auditors have to continue professional education. As a result, we can say that CMB regulations comply with standards in this respect.

Article 9 of the Communiqué regulates the liabilities of independent audit institutions regarding in-house trainings and accompaniment trainings for ensuring professional competence. According to this:

1- *Independent audit institutions subject the assistant auditors who do not have professional experience to traineeship. In this traineeship term, lasting de facto at least for two years, assistant auditors are trained in accounting and theories, standards and methods of independent audit, financial analysis, internal control, data processing, money and capital markets, corporation law, institutional management, commercial law, tax legislation and banking topics for four months. The results of this training are assessed by examinations held by independent audit institutions or relevant professional associations. These courses cannot last less than two hundred hours.*

2- *In the traineeship period, every precaution is taken to enable assistant auditors to work on multiple subjects and in the company of more than one auditor.*

In the Standard, importance of proficiency is stated besides the technical training. As mentioned above, proficiency can be acquired by in-house and accompaniment trainings. According to Communiqué of CMB, assistant auditors undergo training at least for two years. The Communiqué also puts emphasis on accompaniment training whereby assistant auditors are able to work with several experienced auditors to gain professional experience. Therefore, from this point of view CMB rules comply with the standard as well.

The level of education and expertise required to enjoy the independent audit authority is regulated in the 5th and 9th Articles of Law No: 3568

The following conditions are required to become a Certified Public Accountant:

a. *To have at least a B. A. degree in law, economics, business administration, accounting, banking, public administration and political science from a Turkish university, or from foreign universities offering degrees equivalent to their Turkish counter parts, on the condition that this equivalence is ratified by the Higher Education Committee, or to hold a post-graduate degree in one of the disciplines mentioned above, following an undergraduate degree received in a* *different branch.*

b. To work as a trainee for at least three years.

c. *To pass the examination for Certified Public Accountants.*

This condition does not apply to the inspectors of public banks rendering audit services throughout the country, to individuals authorized for inspection in compliance with the relevant legislation, to the applicants who have served in public institutions and establishments after having received such authorizations, and to the individuals who have given lectures in the universities on the above mentioned subjects as members of the teaching staff for a period of at least 8 years. (Law No: 3568; Article 5)

Special conditions to become a sworn-in certified public accountant are regulated in Article 9 of the mentioned Law. Accordingly;

a) At least ten years of experience as a Certified Public Accountant;
b) To pass the Sworn-in Certified Public Accountant examination;
c) To receive a license for practicing sworn-in certified public accountancy.

There are some exemptions stipulated in the same Article. As is mentioned above, one condition to become a Sworn-in Certified Public Accountant is having worked as a Certified Public Accountant for ten years. However,

- Service periods of those individuals authorized for tax inspection at public institutions or establishments beginning from the date they get this authorization.
- Service periods of individuals when they are first degree authorized to sign in accounting units of private establishments that keeps balance book, when they are responsible for the management or financial auditing of accounting.
- Service periods that individuals work in the companies of sworn-in certified public accountancy and a certified public accountancy.

- Service periods of the certified public accountants when they work in a business establishment.
- Service periods of who have been appointed as an instructor, assistant professor or professor in one of the fields of law, economics, finance, accounting, business administration or political science

are considered as service periods spent as a certified public accountant.

In line with the Standard, as per the Law No: 3568, having a B.H. degree in business administration, economics, law and accountancy is necessary to be an independent auditor. Furthermore, assistant auditors have to work as a trainee for at least three years to gain professional experience. By the same token, Law No: 3568 complies with the Standard.

Consequently, we can say that certified public accountancy and sworn in certified public accountancy legislation are considerably in compliance with the generally accepted auditing standards in terms of technical training and proficiency with the exception of continuing professional education. Since this standard is interpreted as requiring the auditor to have formal education, adequate practical experience for the work being performed, and continuing professional education. Although there are regulations regarding the first two conditions, there is not any related to the last one.

There is not comprehensive information regarding the technical training and proficiency of auditors in the banking legislation. Only in the 15th Article of Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks, it is stated that "*the partners and external auditors of the institution to be authorized must have obtained the power to audit pursuant to the provisions of the Law Nr. 3568 and must have the title of sworn-in certified public accountant or certified public consultant registered to relevant professional chamber, or must hold a certificate granting the power to conduct external audit in foreign countries in line* *with the principles of reciprocity stated in article 8 of the Law Nr. 3568 or other provisions".*

In the said Regulation, condition regarding the level of education required for independent auditors is not stated; however, reference is made to Law No: 3568. The Articles of Law No: 3568 examined above concerning technical training and proficiency is also valid for auditors assigned to audit banks. Since the Regulation envisages that independent auditors and shareholders of institution to be granted authority must have the authority to audit and have the title of certified public accountant or sworn-in certified public accountant registered at relevant profession chamber as per the Law No: 3568. Consequently, considering that Law No: 3568 generally complies with Standard, regulations in banking legislation are in line with technical training and proficiency standard.

3.3.2 Standard of Independence in Mental Attitude

The second general standard requires that the auditor have independence in mental attitude during the engagement. Independence impedes relationships that harm the auditor's objectivity. A distinction is made between independence in fact and independence in appearance. An auditor must not only be independent in fact but also avoid actions that may appear to affect independence. If an auditor is perceived as not being independent, users may lose trust in the auditor's ability to report accurately on financial statements. (Messier, 1997: 26)

An independent auditor may plan to audit a company in which he owes common stock. The auditor may be act so morally that he or she would never allow such a relationship to affect independence. Although in this case the auditor may in fact be independent, the third parties may assume that the auditor is not independent. This reluctance on the part of third parties to believe the auditor is independent is why auditors must be independent not only in fact but also in appearance. (Guy et.al., 1999: 23)

The way the auditor is assigned and his/her wage affect auditor's independency. Nowadays in many countries, auditors are assigned by a contract signed between the auditor and company management. Selection of auditor is first approved in general board of stakeholders. If company's executive board does not participate in voting for the selection of members for auditing board and this board appoints auditor, the auditor may keep away from effects posed by the company's management. (Kepekçi, 1998: 16)

3.3.2.1 Sarbanes-Oxley Act and Regulations Concerning Auditor Independency

Auditing scandals, recently experienced in great companies like Enron, WorldCom, Tyco and Xerox and bankruptcies experienced in many important banks in our country, as well showed importance of the independency standard. As a result of scandals experienced in these big companies, in 29 July 2002 "Public Company Accounting Reform Act" called as Sarbanes- Oxley Act was published as a precaution. (Dönmez et. al., 2005: 55)

Sarbanes-Oxley Act aims to protect the investors by increasing the accuracy and reliability of public announcements made by companies due to capital market legislation or other reasons. (Güngör, 2003a: 184) II. Part of Sarbanes- Oxley Act is concerning auditor's independency. Mainly these regulations were made in this respect.

In the 201st Article of Act under the title "Services Outside the Scope of Practice of Auditors", services which auditors should not provide to a client together with auditing activity are set forth as follow;

(1) Bookkeeping or other services related to the accounting records or financial statements of the audit client;

(2) Financial information systems design and implementation;

(3) Appraisal or valuation services, fairness opinions, or contribution-in-kind reports;

(4) Actuarial services;

(5) Internal audit outsourcing services;

(6) Management functions or human resources;

(7) Broker or dealer, investment adviser, or investment banking services;

(8) Legal services and expert services unrelated to the audit; and

(9) Any other service that the Board determines, by regulation, is impermissible. (Sarbanes-Oxley Act, 2002; 27-28)

If the independent auditing company provides one of the services mentioned above to its clients in the period of auditing, this company is considered to lose its independency. However, this restriction is valid only if it is *in the same period* and *to the same auditing client* as well.

With the 202nd Article of Act, auditing committee is empowered to prior approval of the auditing and non-auditing works. Act is trying to fortify this committee by increasing the functions and responsibilities of Auditing Committees of public-held companies. Thus, the Act aims to provide better organization and transparency for both independent and internal auditing processes of companies and to inform the public in great extent about company's financial conditions. (Güngör, 2003a: 186)

Article 203 of the Act arranges the issue of audit partner rotation. Accordingly, " It shall be unlawful for a registered public accounting firm to provide audit services to an issuer if the lead (or coordinating) audit partner (having primary responsibility for the audit), or the audit partner responsible for reviewing the audit, has performed audit services for that issuer in each of the 5 previous fiscal years of that issuer.'' (Sarbanes-Oxley Act, 2002: 29)

According to 204 Article with the title of "Auditor Reports to Audit Committees", each registered public accounting firm shall timely report to the audit committee of the issuer;

(1) all critical accounting policies and practices to be used;

(2) all alternative treatments of financial information within generally accepted accounting principles that have been discussed with management officials of the issuer, ramifications of the use of such alternative disclosures and treatments, and the treatment preferred by the registered public accounting firm; and

(3) other material written communications between the registered public accounting firm and the management of the issuer, such as any management letter or schedule of unadjusted differences.'' (Sarbanes-Oxley Act, 2002: 29)

Article 206 of the Act deals with *conflicts of interest*. According to article, "It shall be unlawful for a registered public accounting firm to perform for an issuer any audit service required by this title, if a chief executive officer, controller, chief financial officer, chief accounting officer, or any person serving in an equivalent position for the issuer, was employed by that registered independent public accounting firm and participated in any capacity in the audit of that issuer during the 1-year period preceding the date of the initiation of the audit." (Sarbanes-Oxley Act, 2002: 30-31)

3.3.2.2 Comparison of the Independent External Audit within Turkey with the GAAS

Arrangements with respect to this standard in the legislation of Capital Markets Board are presented in the Articles 12 and 13 of 2nd part of the Communiqué on the Independent Audit Standards in Capital Markets. (Serial: X No: 22)

In the Communiqué, independency is described as "a *unitary of attitudes and comprehensions which provide the performing of professional activity honestly and impartially*". The 10th Article of Communiqué reads "*independent auditors, besides being independent, honest and impartial in independent auditing study, should avoid* *special situations those may annihilate their independency. Moreover, the auditors should act with professional skepticism and avoid conflicts of interests during their studies, demand help from their superiors and if necessary from Board to provide the solution of ethical conflicts they come across, rule out any intervention that may effect their honesty and impartiality, explain their opinions, which they reached in consequence of independent auditing, disregarding others' direct or indirect benefits".*

According to the independence in mental attitude standard, independent auditors should be independent both in real and in appearance during their auditing studies. In the Standard, it is stated that independent auditors should avoid the situations that would cause any doubt in public about their independency. The Communiqué of Capital Markets Board deals with the issue of independency in detail. As in the case of standard, CMB's relevant Communiqué stresses the issues of auditors' independency in their auditing studies and requires them to avoid the situations that would damage their independence. Consequently, CMB regulations are in the same path with the independence standard.

In the Article 13 of mentioned Communiqué', situations that may annihilate the independence are determined as follow:

a) Authorities of independent auditing institutions and their relatives up to third degree;

- *Having a direct or indirect benefit from client or a commitment for providing a benefit to them.*
- *Having a direct or indirect partnership relation with a client.*
- *Having worked for client or in a work relevant with him.*
- *Having loan-credit relation with client or any of his subsidiaries.*

b) Non-payment of past years' independent auditing fees by client without a valid reason.

c) Fee of independent audit, being conditioned with the results of independent audit or having clear differences from market value.

In the existence of above-mentioned situations, it is considered that independence of auditor is annihilated. Besides, *independent auditors can not occupy the positions of chairman and members of board of directors, a general manager, a manager and a assistant manager in the companies in which they have actually performed an independent audit, unless two years pass over the date of last independent audit report prepared about financial statements of that company.*

Also in the Communiqué, the services, which should not be provided by auditors to the same client during the auditing activity, are mentioned. These are;

1) *Recording books of account and providing other relevant services,*
2) *Setting and developing financial information system, providing consultancy services concerning implementations about business administration, accounting, finance, issuing documents and preparing reports,*
3) *Providing assessment and actuary services or preparing expertise and compliance reports,*
4) *Fulfilling internal auditing function or providing supportive service for internal auditing function,*
5) *Fulfilling management or human resources function,*
6) *Providing brokering or investment consultancy services,*
7) *Providing legal consultancy or other expertise services,*
8) *Arbitration and expertise services,*
9) *Providing services in the scopes which Board does not let,*

There is an exception of the services, which auditors should not provide to the same client together with auditing activity. According to this; in the framework of Law No: 3568; activities like examining the compliance of financial statements and declarations with tax legislation provisions and certifying the compliance, giving written opinion about subject and preparing report, are not considered in the scope of prohibited activities mentioned above.

Finally, *a consultancy company mastered by independent auditing institution directly or indirectly, can not provide consultancy service to the client at the same period.*

As the situations annihilating independency were restricted with traditional issues like providing benefit, partnership relation, management relation before Sarbanes-Oxley Act, they are rendered compliant with Sarbanes-Oxley with the amendment dated 02 November 2002, valid after 01 January 2003.(Güngör, 2003b: 217) Services in CMB's Communiqué, which auditors should not provide to the same client at the same period with auditing activity, are mostly similar to those provided for in Sarbanes-Oxley Act.

Explanations concerning independency standard are covered in the 45th and 48th Articles of Law No: 3568 and in the 9th and 43rd Articles of Regulation on the Working Methods and Basis of Certified Public Accountants and Sworn-in Certified Public Accountants.

According to the 9th Article of said Regulation, *profession members perform their studies independently under their own responsibilities. Independency is fundamental and indispensable element of the profession*. In addition, it is stated that *profession members should avoid the relations and behaviors those can affect their independency.*

Arrangements regarding the situations that can annihilate or damage auditor's independency are made in the 45th Article of Law No: 3568 and 43rd Article of the Regulation. According to this:

"*Member of profession by using their title and the authorization for certification may not serve real and legal personalities and may not be employed in their offices on the basis of contract for purposes of performing the works; may, not* *become involved in commercial enterprises and may not perform deeds that contradict the honor and dignity of the profession.*

Sworn-in Certified Public Accountants may not become engaged in the business affairs of their spouses (even if divorced), their parents, children, and their relative and relatives to the third level (included), and the firms of which such persons are partners; and may not certify the transactions carried out by sworn-in Certified Public Accountants who have become involved in the affairs of their relatives with the above mentioned kinship ties." (Law No: 3568; Article 45)

In the 43rd Article of the Regulation, it is stated that *profession members can not attend commercial activities, posses the position of partner in sole proprietorships, member and chairman of board in capital stock companies.*

The 48th Article of Law No: 3568 regulates the disciplinary penalties. Accordingly, "*members of profession those who fail to perform their duties independently, objectively and honestly, or those who act contrary to the general principles of this profession are penalized by the sanction of temporary withholding of professional activities*."

Although there are arrangements concerning the independency of auditors in certified public accountancy and sworn in certified public accountancy legislation, it is not sufficient. Comprehensive arrangements with respect to implementation were not made. Contrary to CMB's legislation, arrangements made in this legislation are not in parallel with Sarbanes Oxley Act. Therefore, we cannot say that arrangements in certified public accountancy and sworn in certified public accountancy legislation are the same with the standard.

In the 12th Article of Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks, there is a comprehensive explanation on the auditor independency and the situations that annihilate the independency. In the Regulation, independency is defined as "the *total of the behaviors and* *understandings that will ensure that the partners, chairman and members of the board of directors, auditors and managers of the authorized audit institutions and the external auditors employed by them execute their professional activities within the framework of the principles of integrity, impartiality and professional skepticism".*

It is further stated that "*external auditors are obliged to keep away from any relationship of interest that may arise during their activities, not to allow any intervention that may affect their integrity and impartiality, to disclose their opinions which they have reached as a result of external audit in their reports without giving consideration to direct and indirect interests of themselves or of others*".

The same Article specifies the actions that may annihilate the independency. Arrangements on this subject are similar to those in the CMB regulations. Since the arrangements in this regard are explained widely above in CMB part, it will not be discussed again.

Also, in the Article it is stated that "*authorized audit institution and partners, chairman and members of the board of directors, auditors, managers and external auditors and their relatives both by marriage and by blood and other institutions established in Turkey which have a legal connection with the said institutions may not render the following services to the bank they audit or to the partnerships controlled directly or indirectly by the bank*;

1) Designing and implementing financial information system,

2) Preparation of expert's report,

3) Rendering actuarial services,

4) Rendering services related with management or human resources management,

5) Rendering investment advisory services".

Auditor independency and the situations that annihilate the independency are specified comprehensively in Banking Regulation and Supervision Agency arrangements and it is stated therein that auditors should be independent in auditing study and avoid the situations that might affect their independency. As a result, we can say that BRSA's arrangements are in the same course with independency standard.

In BRSA's Regulation, the services that should not be provided to the same bank with auditing activity are specified, although it is not as broad as it is in Sarbanes Oxley Act. Therefore, we can regard the arrangements in BRSA to be in line with Sarbanes Oxley Act.

3.3.3 Standard of Due Professional Care

The third general standard requires due professional care in the conduct of the audit and in the preparation of the audit report. This standard requires the auditors to plan and carry out every step of the audit engagement in a careful and diligent manner. (Whittington and Pany, 2001: 36) Due care means that the auditor performs his or her duties with a degree of skill commonly possessed by others in the profession. (Meisser, 1997: 26)

Auditing profession is the one that requires due professional care during auditing study and in the phase of reporting, following the auditing standards fully, using knowledge, experience and skills in the most efficient way. (Kepekçi, 1998; 17)

Exercise of due care calls for auditors to fulfill the requirements of all other standards. They must properly plan the audit, examine sufficient evidence, evaluate the financial statements and carefully prepare the report containing their opinion. (Cook and Winkle, 1988: 38)

3.3.3.1 Comparison of the Independent External Audit within Turkey with the GAAS

Regulations concerning this Standard in Capital Market Board are determined in the 14th Article of 2nd part of Communiqué on Independent Auditing Standards in Capital Markets.

In the 14th Article of the Communiqué, due professional care is described as *"attention and effort which a prudent auditor would show under the same circumstances"*

We can say that this subparagraph of CMB Communiqué matches up with the Standard because in standard, due care is described just as it is in Communiqué.

In the following of Article, it is mentioned that *independent auditors should take the necessary professional care in the phase of planning, performing and concluding independent audit and in preparing the independent audit report. Also, it is indicated that following the independent audit standards completely is the minimum yardstick of due professional care. Therefore, the auditor should plan the auditing activity as required, make programme, make examination by collecting sufficient, suitable and reliable auditing evidence, prepare clean and regular working papers, achieve an honest and correct judgment about the reality and accuracy of financial statements and declare his opinion in the independent audit report that he/she would prepare with care and particularity.*

According to Standard, auditors must properly plan the audit, examine sufficient evidence, evaluate the financial statements and carefully prepare the report. Almost the same phrase was used in the CMB Communiqué. Therefore, we can say that CMB regulations are in parallel with mentioned Standard.

In Law No: 3568, there is not any arrangement concerning the standard of due professional care. Only in the 6th Article of Regulation on the Working Methods and Basis of Certified Public Accountants and Sworn-in Certified Public Accountants concerning honesty, impartiality and reliability, it is specified that *"Members of profession should avoid the conflicts of interest during their studies and show the necessary due professional care when performing their duties."*

The concept of due professional care stated in the Regulation and the one explained in Standard have different meanings. While according to Standard, due professional care means planning of auditing activities in a good manner, collecting valid and reliable evidences in sufficient numbers and preparing audit report by achieving an accurate audit opinion; due professional care is expressed in Regulation as an attitude that auditor should show to ensure his/her independency. Consequently, we can say that the arrangements in certified public accountancy and sworn in certified public accountancy legislation are not sufficient and fall behind in meeting the standard.

According to 11th Article of Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks, *external auditor are obliged to show professional diligence and care while executing their activities, as well as all responsibilities for not harming their independence, integrity and impartiality, confidentiality, professional skepticism and professional reputation and for acquiring and maintaining professional qualification.*

Thus, professional care standard is not covered in banking legislation; however, it is specified that external auditors should show professional care and attention during auditing. In this context, we can not say that BRSA's arrangements comply with the Standard.

3.4 Standards of Fieldwork

Auditing study basically depends on evidence collection and evaluation of them. The fieldwork standards divides the rules that should be observed for making a qualified auditing study and achieving an accurate audit opinion under three groups. (Kavut, 2000: 15) These standards address planning and supervision, internal control, and sufficient competent evidential matter as follow:

1. The work is to be *adequately planned* and assistants, if any, are to be *properly supervised.*

2. A *sufficient understanding of the internal control structure* is to be obtained to plan the audit and to determine the nature, timing, and extent of tests to be performed.

3. *Sufficient competent evidential matter* is to be obtained through inspection, observation, inquires and confirmations to afford a reasonable basis for an opinion regarding the financial statements under examination. (Meigs et.al., 1989: 20)

3.4.1 Standard of Planning and Supervision

The first standard of fieldwork envisages well-planned audit study and ably supervision of the assistant auditors, if any. Basic elements of audit planning are allocation of human resources, time planning and efficient resource usage planning. (Güredin, 1997: 29) In planning, it is necessary to divide audit into fields in the first place and then, to determine the auditing methods and processes to be applied to each auditing field. (Kavut, 2000: 16)

The auditor should acquire knowledge about the industry in which the client operates. The auditor should understand how the industry is affected by economic conditions, tax laws and other government regulations. Moreover, adequate planning includes the auditor's acquiring an understanding of the nature of the client's business, its organization, the location of its facilities, the products sold or services rendered, its financial structure, related party transactions, methods of compensation and other matters. (Cook and Winkle, 1988: 40)

To acquire the necessary knowledge for planning, the auditor makes use of any prior experience with the client company. Much useful information may be obtained from the working papers of prior audits. Publications, textbooks, industry trade journals, discussions with the audit committee and management personnel of the client's company can be an important source of information. Additionally, a review of interim financial statements on the current year may alert the auditor to matters affecting audit plans. Assistance expected from internal auditors will also influence the planning. (Cook and Winkle, 1988: 40)

In the second part of this standard, directing and controlling the studies of assistant auditors who will take place in auditing team is stipulated. Assistant auditors do not have the professional education and experience of a senior auditor. This standard also has an important function in the practical training and specialization of assistant auditors. (Kavut, 2000: 16)

Assistant auditors try to fulfill their tasks in accordance with auditing programmes within the instructions given by responsible auditors. Road map for collecting necessary audit evidence is given in detail in auditing programmes. Assistant auditors frequently refer to the senior auditor. There are no certain rules about the limits of the responsible senior auditor's custody over his/her assistants. However, the scope of this custody depends on assistant auditor's general and professional knowledge level, assistant auditor's experience in topic and the difficulty and complexity of auditing topic. (Güredin, 1997: 30)

3.4.1.1 Comparison of the Independent External Audit within Turkey with the GAAS

Explanations concerning planning and supervision standard are pointed out in the 9th part of CMB's Communiqué on the Independent Audit Standards in Capital Markets.

In the 4th Article of Part 9 of the Communiqué, it is stated that *auditor should make planning in order to realize an efficient independent audit study.* It further highlights, "*Planning of audit includes development of audit plan and determination of audit strategy. In order to increase the efficiency of planning process, responsible common senior auditor and the other important members of independent audit team are incorporated into planning.*"

In the said Article, particular planning activities, which independent auditor should complete during planning independent audit, are mentioned. In this scope, independent auditor determines and evaluates:

- *Negotiations among the members of independent audit team;*
- *Analytic examination methods which would be fulfilled in risk assessment;*
- *General information acquisition about the legal and regulating framework effecting enterprise and how the enterprise adapts the mentioned framework;*
- *Determination of significance level;*
- *Situations which require expert opinion;*
- *Appreciation of important failure risks.*

In the standard, it is mentioned that a good audit begins with a planning and to make planning, there needs to be information on the legal and regulatory framework of the industry in which the audited company operates. There is considerably broad explanation on planning in CMB's Communiqué. In the Communiqué, planning is even covered in a much wider scope than it is in generally accepted auditing standards. However in general sense, importance of planning and planning activities are touched upon in capital market legislation as in the case of Standard. In this context, arrangements in CMB legislation are in accord with Standard.

In the 20th Article of Communiqué's 2nd part under the title "Supervision and Coordination", it is stated *"common principal auditor is responsible for implementation of independent audit programme, sufficient and efficient supervision and coordination of independent audit study. This responsibility contains informing and conducting independent auditors about the activity, clear determination of duties and responsibilities of these people, frequently review of the performed activity through the process, providing the necessary recording in order to solve the problems appearing in studies and following the activity from working papers."*

Besides, *independent auditors, who are assigned to control the independent audit, examine the assessments of the audit team about independency in the framework of significance notion concerning the determination of risks and supervise independent audit study by examining the reports and working papers, the negotiations with managers who are responsible for implementation of institutional management principles.*

In the Standard, it is stated that assistant auditors, who would take place in auditing team, should be guided and supervised by senior auditors. In CMB's relevant Communiqué, responsible common principal auditors are held responsible for supervision, coordination and control of independent audit studies. Consequently, CMB's arrangements are consistent with the Standard in this aspect.

In certified public accountancy and sworn in certified public accountancy legislation, planning standard is regulated in the 53rd Article of the Regulation on the Working Methods and Basis of Certified Public Accountants and Sworn-in Certified Public Accountants. According to this; *" auditors make planning by taking into account the general information about the company, its human resources, accounting department, sales, inventory, cost system, condition of fixed assets, situation of* *company's debts and credits, relations with tax office and other official institutions, balance sheet and statement of income."*

The said Article further reads *"audit begins with the authorized profession member's preparation of a written audit program which contains audit's time process, number of staff assigned in audit, whether or not to benefit from internal control organization and subjects focused on audit."*

Even though there is not a wide explanation as in the case of CMB's legislation, in certified public accountancy and sworn in certified public accountancy legislation, subjects that should be considered when planning are specified. In addition, it envisages to initiate an audit by planning. We can say that it is in general consistent with the Standard.

Concerning the control of audit, the 54th Article of the said Regulation reads *"Members of profession should perform control and planning, in an efficient and sufficient way in every phase of audit. Conduction of studies of staff which assigned in auditing activity and conclusion of audit consistently with its goal are tasks of member of profession who shoulders the audit responsibility."*

In the second part of planning and supervision standard, it is stated that the studies of assistant auditors in auditing team should be guided and controlled. Said Regulation emphasizes as well that the auditor who takes the responsibility of audit, guides and supervises the studies of assistant auditors who are assigned in audit. As is seen, certified public accountancy and sworn in certified public accountancy legislation is in consistency with this part of the Standard.

The 6th part of Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks deals with planning. Planning of independent audit include setting of an audit strategy and development of audit plan. In the 28th Article of Regulation titled "Audit Strategy", it is stated that "*The board of directors of the authorized audit institution shall settle a general management strategy outlining the allocation of human resources, including the appointment of external auditors with* *adequate experience in issues involving a high risk or using the assistance of experts in respect of related issues and the administration and management of resources required for special audit areas and how the process will be monitored in respect of the scope and timing of an external audit and important issues that should be considered during the audit process by taking account of the sufficiency of internal systems of the bank.* ”

Standard of planning and supervision requires the ably planning of audit study and custody of assistant auditors if they exist. In the Standard it is stated that basic elements of audit planning are human resource planning, time planning and planning of resources. In the mentioned Regulation it is stated that authorized audit institution shall settle audit strategy which contains the allocation of human resources, administration and management of resources and how the process will be monitored in respect of the scope and timing of an external audit. In this context we can say that regulations in banking legislation match up with Standard. However, there is not explanation regarding the second part of the Standard. The supervision of assistant auditors is not mentioned so we can not say that regulations of banking legislation fully match up with Standard.

3.4.2 Standard of Internal Control

The second standard of fieldwork requires the auditor to obtain a sufficient understanding of internal control. Better internal controls increase the probability that financial data are reliable and reduce the amount of evidence the auditor must collect through other audit tests. Conversely, weaker internal controls indicate a higher probability of less reliable financial information and increase the amount of evidence the auditor must collect through other auditing procedures. (Guy et al., 1999: 24)

According to this standard, there are three reasons for examination of internal control system of the audited company. The first reason for the study is to establish reliance on the control structure itself. Auditors cannot reconstruct the records for all transactions that have taken place during the period under audit. Therefore, they must be able to trust on the dependability of the accounting system with its controls for the proper recording of transactions and the production of financial statements reflecting those events. Auditor's confidence to the efficiency of the operating system would decrease the audit risk. (Başpınar, 2005: 56)

The second purpose of the examination of the control structure is to help in the design of auditing tests the auditor must make to be satisfied about the fairness of financial statements. The plan for audit is affected by the strengths and weaknesses of the company's control procedures. An effective control structure greatly increases the possibilities that resulting financial statements will be accurate. Since auditing procedures are affected by the degree of risk involved, it is evident that strong control procedures reduce the risk of errors in the financial reports and so reduce the extent of auditing procedures required. (Cook and Winkle, 1988: 44)

Another reason for reviewing the client's control structure is to enable the auditor to inform the client of weaknesses in procedures and perhaps to make recommendations for improvements. The auditor can place greater reliance on the control procedures for the remainder of the period under examination if these recommendations are implemented. Auditors should communicate any material weaknesses in the controls that come to their attention to both senior management and the board of directors. (Cook and Winkle, 1988: 44)

3.4.2.1 Comparison of the Independent External Auditing within Turkey with the GAAS

Information concerning internal control system is given in the Article 11, Part 10 of CMB's Communiqué on the Independent Audit Standards in Capital Markets. It is stated that *independent auditor should grasp internal control system; because he/she would benefit from the information concerning internal control system to determine the important error kinds, to assess the risks and decide timing of additional independent audit techniques.*

In the 11th Article, *internal control system is described as a system designed and implemented by company management for providing a reasonable guarantee concerning enterprise achieved goals, activities and operations realized efficiently and that laws and regulations are obeyed. For this purpose, internal control system is designed and implemented so as to reveal the operation risks which appear as a threat in the aspect of realizing the goals.*

Additionally in the Communiqué, it is stated that the subject that auditor should primarily consider is *the efficiency of internal control system, whether it is capable of preventing, revealing, and correcting major mistakes in types of transaction, balance of accounts, footnotes and the statements made by relevant company management.*

Examination and assessment of internal control system and reliability testing are required in the standard of internal control, as effectiveness of internal control system increases the accuracy and reliability level of financial statements. In addition, in CMB's Communiqué it is pointed out that internal control system should be analyzed and evaluated. It further envisages that efficient internal control system provides a reasonable guarantee that business objectives are achieved, activities and procedures are efficiently realized, laws and regulations are observed. Consequently, arrangements in the Capital Markets Board comply with the Standard.

Explanation concerning internal control standard is not included in certified public accountancy and sworn in certified public accountancy legislation. Solely in 52nd Article of the Regulation on the Working Methods and Basis of Certified Public Accountants and Sworn-in Certified Public Accountants, it is stated that information should be obtained regarding internal control system of audited enterprise, and in 53rd Article, it is pointed out that information gathered should be considered in the planning of audit.

As is seen there is no arrangement comparable to internal control standard in certified public accountancy and sworn in certified public accountancy legislation.

Explanation concerning internal control system is given in the 35th Article of Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks. In the Article, it is stated that auditors "*shall understand the design and operation of the internal control system and determine whether it is capable of preventing, revealing, and correcting the risk of a materially misleading statement.*"

Said Article further stipulates that *auditors make an assessment of the functioning of the internal control system to understand whether the bank has an internal control system and whether such system is working sufficiently. An internal control system designed improperly shows the internal control system of the bank is insufficient, and it shall be reported by the external auditor to the board of directors of the bank.*

Auditors, when obtaining audit evidence during a risk assessment process through controls in the internal control system:

- *make interviews with personnel of the bank,*
- *supervise certain control procedures,*
- *review reports and documents,*
- *monitor information system processes related to financial reporting*.

According to the Standard, examination and assessment of internal control system and test of its reliability are necessary. Also in BRSA's Regulation, it is specified that internal control system should be examined and assessed, and evaluated whether it has the capacity of preventing, revealing, and correcting the risk of a materially misleading statements. Consequently, we can say that BRSA's arrangements comply with the Standard.

3.4.3 Standard of Sufficient Competent Evidential Matter

The third standard of fieldwork requires the collection of appropriate, reliable and sufficient evident via such auditing techniques as observation, affirmation, investigation and document analyzing to support the audit opinion on the financial statements of audited enterprise. Auditor would determine the quantity of evidence according to the efficiency of enterprise’s internal control system. (Aksoy: 2002; 118)

The sufficiency of evidential matter relates to the quantity and quality of information required to support an auditor’s opinion. When determining whether evidence is sufficient, the auditor must exercise professional judgment as to how much and what kind of audit evidence is needed, based on the nature of the item under examination, the materiality of possible errors and fraud, the degree of risk involved, and the kinds and competence of evidential matter available. An experienced auditor rarely collects enough evidence to be convinced beyond all doubt of the fairness of every aspect of the financial statements audited. The auditor must decide whether the evidential matter available is sufficient to support an opinion that the financial statements are fairly presented in conformity with generally accepted accounting principles. (Guy et al., 1999: 25)

For audit evidence to be competent, it must be both valid and relevant. Evident is determined more valid when it is obtained by the auditor from independent parties outside the client’s organization, when it is developed under satisfactory internal accounting controls and when it is gathered directly by the auditor rather than indirectly. (Cook and Winkle, 1988: 45) For the evidence to be relevant, it must apply to the audit objective and assertion being tested. Therefore, if attempting to gather evidence that accounts receivable is fairly stated, the auditor must obtain evidence that applies to accounts receivable. (Guy et al., 1999: 25)

Audit evidence can be prepared and given to auditor by the audited company or the auditor can gather evidence inside or outside the company by applying various audit procedures. Evidence can be classified according to their sources as follows: (Güredin; 1997: 31-32)

- Evidence collected by auditor’s physical examination with a view to determining their physical existence; for instance, determination of the physical existence of inventories.

- Evidence collected by the observation of auditor with a view to determining whether instructions issued by management are followed; for instance, determining whether the security precautions that are stipulated to protect the assets against theft are applied or not.

- Oral statement of people outside the company under audit; information concerning a specific juristic situation received by the auditor from the lawyer of client company ;

- Oral statements from client company and from workers; for instance, oral information on company’s internal control system, information concerning company’s sale policy and journal entries.

- Documentary evidence prepared inside the company. Sale invoices, order bills, receipts, standard accounting slips.

- Documentary evidence prepared outside the company, sent to client and kept in client’s files; for instance, bank statements and bank receipts.

- Documentary evidence prepared and directly sent to auditor from external sources. Bank statements directly posted to auditor, letters or confirmations directly sent to auditor by the institutions that are in business relation with the audited company.

- Analytical evidence prepared by auditor. Re-calculations made by the auditor to check the accuracy of arithmetic operations and transfers, ratio analysis, trend analysis, and regression analysis.

3.4.3.1 Comparison of the Independent External Auditing within Turkey with the GAAS

Part 14 of Capital Markets Board's Communiqué on the Independent Audit Standards in Capital Markets exclusively deals with the subject of independent audit evidence. In the 3rd Article of 14th Part, independent audit evidence is described as such: *all information used by independent auditor to achieve the conclusions which his/her opinion depends on, including information in accounting records. Independent audit evidence is cumulative and includes the evidences gathered by independent audit techniques implemented during independent audit, and also may include evidences from other sources like former independent audits.*

According to the provisions of this Article, the independent auditor *collects independent audit evidence by testing accounting records with some procedures like analyzing, reviewing, repeating similar operations and comparing relevant information and, as a result of independent audit techniques he/she applied, decides whether the accounting records are consistent and coherent with financial statements or not.*

According to the Communiqué, *auditor collects audit evidence by using independent audit techniques like, decisions made in meetings, confirmations with third party, analyzing reports, comparing with competitors, control of procedures performed by manual system, observation and research.*

In Article 4 of said Part under the title "Sufficient and Appropriate Independent Audit Evidence", *sufficiency is described as measure of the amount of independent audit evidence; and competence is described as measurement of the* *quality of independent audit evidence. It is specified as well that reliability of these evidence helps to determine the important mistakes in account balances, footnotes and the explanations made by company management to public.*

It is specified in this Article "*quantity and quality of independent audit evidence is affected by important error risk, higher risk necessitates higher quality in independent audit evidences. Besides, sufficiency and competence of independent audit evidence are relevant with each other. On the other hand, just collecting more independent audit evidence does not compensate independent audit evidence's low quality".*

Mentioned Article stipulates as well that the sources of evidences affect the reliability of evidence. Accordingly;

1) Independent audit evidence gathered from independent sources outside the company is more reliable.

2) Independent audit evidence gathered from companies having an efficient internal control system is more reliable.

3) Independent audit evidence obtained by independent auditor directly through the observation of control implementation is more reliable than those obtained indirectly.

4) Independent audit evidence collected from records is more reliable. In this context, independent audit evidence obtained from meeting minutes kept continuously is more reliable than those that are orally stated.

5) Independent audit evidences from original records and documents are more reliable than the ones obtained from photocopies and faxes.

Standard of Sufficient Competent Evidence requires the collection of competent, reliable and sufficient evidences by means of audit techniques like observation, affirmation, investigation and document analyzing for the auditor to establish his/her view about client's financial statement. Likewise, in the Communiqué of CMB, it is emphasized that while constituting audit view, auditor should obtain sufficient, competent and reliable audit evidence by using independent audit techniques like analysis, review, repeating similar procedures, comparing relevant information and attestations through third parties. Besides, in CMB's Communiqué, the importance of sources for determining the reliability of evidences is stressed as it is in Standard. Consequently, we can say that CMB's arrangements are in the same path with Standard.

In certified public accountancy and sworn in certified public accountancy legislation, explanations concerning evidence collection standard are covered in the 14th and 15th Article of Regulation on Documents Certified by Sworn in Certified Public Accountants, Certification Issues, Basis and Principles of Certification and in the 55th Article of Regulation on the Working Methods and Basis of Certified Public Accountants and Sworn-in Certified Public Accountants.

In the 14th Article of Regulation on Documents Certified by Sworn in Certified Public Accountants, Certification Issues, Basis and Principles of Certification, under the title of "Evidence Collection", it is stated that Sworn in Certified Public Accountants should collect sufficient and reliable evidence concerning the subject and scope of certification while performing certification studies.

Evidence are collected to determine,

a) Whether or not all assets, sources, incomes and expenditures are real and all operations concerning these are truly recorded;

b) Whether or not all operations and accounts which should be reflected on financial statements are fairly presented in these statements;

c) Whether or not the rights concerning assets and liabilities belong to company.

The audit techniques, which Sworn in Certified Public Accountancies would apply while performing audit activities, are regulated in the 15th Article of said Regulation. During certification studies, Sworn in Certified Public Accountants *collect the evidences by inventory analysis, document analysis, information gathering, affirmation, comparison, scoring and analytical research.*

In the 55th Article of Working Regulation, it is stated that *profession members should perform studies like financial audit, balance sheet audit, income statement audit, tax audit, financial analyzing of statements, control of coherence between balance sheets and accounting records, control of coherence between balance sheet items and the standard form of them for purpose of gathering and assessing the necessary information and documents for determining whether the assets, sources, incomes and expenditures in the financial statements of foundations and institutions reflect the reality or not and whether they are recorded truly or not.*

In the Regulation on Certification, it is stated that sufficient, competent and reliable evidence should be collected before certification of financial statements; and in Working Regulation, it is stated that necessary information and documents should be collected while searching the accuracy of information in financial statements. Furthermore, in Certification Regulation, audit techniques used for collecting evidence are emphasized. Generally assessing issue in the framework of certified public accountancy and sworn in certified public accountancy legislation, implementations in Certification Regulation are more coherent with Standard, because in Working Regulation sufficiency, reliability and competency of evidences to be collected are not mentioned. Consequently, we can say that certified public accountancy and sworn in certified public accountancy legislation is coherent with Standard though not exactly.

In banking legislation, arrangements concerning collection of evidence are made in the 31st Article of Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks. In the Article, it is stated that *the external auditor shall form his opinion by gathering and assessing adequate and reliable audit evidence by using auditing techniques*.

In the Article, the aim of gathering external audit evidence is stipulated. External audit evidence is gathered to verify that;

1) All assets, resources, incomes and expenses in the financial statements are true and all transactions related to them have been recorded accurately based on their actual amounts;

2) Rights and liabilities are true,

3) Valuations have been made in accordance with accounting and valuation procedures set forth in the applicable regulations;

4) The financial statements contain descriptions, classifications, and explanations as of the main items.

In addition, an external auditor shall decide whether the audit evidence is sufficient and relevant by giving consideration to:

1) The criticality level determined by the audit strategy,

2) The functioning and adequacy of the internal systems of the bank in terms of the coherence and reliability of financial statements,

3) Experience gained during audits conducted in the past, *4) The outcome of audit techniques applied and cases of misconduct or errors discovered by using those audit techniques;*

5) The reliability of existing information.

According to same Article, evident *is determined more reliable when it is obtained from external sources than those provided by the bank, institutions with effective accounting and internal systems, documented audit evidence than verbal statements, the originals of documents than their copies and by using audit techniques applied by an external auditor than those obtained indirectly.*

In the mentioned Article, it is stated that *auditor shall give a qualified opinion or states that he is unable to form an opinion by citing related reasons if the external auditor cannot obtain adequate and appropriate evidence for forming an opinion.*

Article 33 of mentioned Regulation is pertinent to *audit techniques used for gathering evidence. An external auditor shall gather adequate audit evidence in the required number by using all or some of the following techniques; physical examination, observation, verification, gathering information, monitoring of the recording system, recalculation, review of documents, an analytic examination, sampling, verification and obtaining confirmation*.

In the mentioned Regulation of BRSA, detailed studies concerning the collection of evidence are performed. In the Regulation, goals of collecting independent audit evidence, issues affecting the sufficiency and competency of evidence, evidence from which sources are reliable and the audit techniques for collecting evidences are pointed out. We see that the arrangements in banking legislation touch upon almost all issues mentioned in the Standard. Consequently, we can say that it is accordant with the Standard.

3.5 Standards of Reporting

For many users of financial statements, an auditor's report is the only evidence that a professional examination has been made. Consequently, it is extremely important that the report be prepared in a professional manner. (Cook and Winkle, 1988: 46)

Standards of reporting address generally accepted accounting principles, consistency, disclosure and expression of an opinion as follows: (Guy et al., 1999: 25)

1. The report shall state whether the financial statements are presented in accordance with generally accepted accounting principles.

2. The report shall identify circumstances in which such principles have not been consistently observed in the current period in relation to the preceding period.

3. Informative disclosures in the financial statements are to be regarded as reasonably adequate unless otherwise stated in the report.

4. The report shall contain either an expression of opinion regarding the financial statements taken as whole or an assertion to the effect that an opinion cannot be expressed.

3.5.1 Standard of Generally Accepted Accounting Principles

Presentation in accordance with generally accepted accounting principles is the requirement of the first standard of reporting. Since the auditor is expressing an opinion that the financial statements fairly present a client company's financial position, cash flows, and results of operations, the auditor must establish a criterion for measuring fairness. The presently accepted measure is generally accepted accounting principles. This term covers those conventions, rules and procedures that define accounting practices accepted at a particular time. Auditor, by examining client company's financial statements, searches whether generally accepted accounting principles are obeyed or not while preparing statements. (Cook and Winkle. 1988: 46)

3.5.1.1 Comparison of the Independent External Auditing within Turkey with the GAAS

In the 3rd Article of Part 30 of Capital Markets Board's Communiqué on the Independent Audit Standards in Capital Markets, it is stated that *auditors shall clearly declare in independent audit opinion whether financial statements reflect the reality in all important aspects in accordance with financial reporting standard or not.*

According to CMB's regulations auditor should clearly state in his/her opinion whether financial statements fairly reflect the reality in all important aspects in accordance with **financial reporting standards**. Nevertheless, according to standard of generally accepted accounting principles, it should be clearly stated in auditor opinion that whether or not financial statements are prepared in accordance with **generally accepted accounting principles**. As is seen, there is an inconsistency between Standard and CMB arrangements. While in CMB arrangements, compliance of financial statements with financial reporting standards is sought, in the Standard it is searched whether they are in accordance with generally accepted accounting principles. In this aspect, CMB's arrangements are not coherent with the Standard.

In Communiqué on Independent Audit in Capital Markets which was abolished with the Communiqué on the Independent Audit Standards in Capital Markets, it was stated that in auditor opinion, it should be explained whether financial statements are prepared in accordance with generally accepted accounting principles. However, in the justifications of Communiqué on Accounting Standards in Capital Markets, it is stated that studies for adaptation of Accounting Standards to

International Financial Reporting Standards (IFRS) are accelerated, because European Union requires companies' consolidated financial statements to be prepared in accordance with IFRS. Therefore, CMB promised to put IFRS into practice in the Letter of Intend presented to International Monetary Fund on 30.07.2002.

Furthermore, with the Norwalk Agreement signed on 18.09.2002 between Accounting Standard Board (ASB) and Financial Accounting Standards Board, it was agreed that the differences between IFRS and Generally Accepted Accounting Principles would be eliminated and high quality and compatible accounting standards that would be used both in national and international financial reporting would be developed. (Legal Ground of Communiqué on Accounting Standards in Capital Markets; Serial XI, No: 25) Consequently, it will not be a right expression to say that CMB's arrangements are not coherent with Standard, because as indicated above IFRS and Generally Accepted Accounting Principles are tried to be adapted.

There is no explanation in certified public accountancy and sworn in certified public accountancy legislation. Only in the 48th Article of Working Regulation, auditing is described as a systematic study which researches and approves by evidences whether or not the real nature of economic activities are reflected in the records in accordance with relevant legislation and *generally accepted accounting principles*. However, the reporting part of the Regulation does not cover the issue to search for the compliance of financial statements with generally accepted accounting principles. Consequently, we cannot say it is coherent with Standard.

According to the 47th Article of BRSA's Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks, there should be an explanation in the audit report that *financial statements are drawn up and submitted in accordance with the Turkish Accounting Standards; and Turkish Financial Reporting Standards and other regulation, communiqué and circulars published by the board on accounting and financial reporting principles and announcements made by the Agency.*

Also in banking legislation, as it is in CMB's legislation, it is stated that explanation should be made concerning whether or not financial statements are prepared in conformity with financial reporting standards, not according to generally accepted accounting principles. In this situation, we have to say that arrangements in banking legislation are not coherent with the Standard, but as explained in CMB part, there are ongoing studies to adopt IFRS and GAAP to each other. Consequently, we can say that arrangements in banking legislation are quite coherent with Standard.

3.5.2 Standard of Consistency

The second standard of reporting is consistency principle. According to this standard, it should be clearly stated in auditor's report that accounting principles are implemented in this term without any change as in the case of previous term. (Güredin, 1997: 34)

Consistent application of accounting principles from period to period is necessary for users to know that all significant changes in financial statements over time result from business activities and not from changed accounting principles. (Cook and Winkle, 1988: 47)

During audit study auditor searches whether there is a deviation from the principles and methods implemented in previous term or not. Auditor does not state in his/her report if there is no change according to previous term; if any, however, the auditor should state these changes in his/her own report, even if management explains the changes in footnotes of financial statements. (Kepekçi, 1998: 19)

3.5.2.1 Comparison of the Independent External Auditing within Turkey with the GAAS

There are provisions concerning consistency standard in the 3rd Article of Part 31 of CMB's Communiqué on the Independent Audit Standards in Capital Markets. According to the Communiqué, *independent auditor should obtain sufficient and* *appropriate independent audit evidence to ensure that comparative financial statements are compatible with financial reporting standards. Independent auditor should consider whether the previous term accounting policies are consistent with current term policies or whether appropriate corrections and/or explanations are made or not.*

Besides, in the 44th Article of Communiqué on Principles and Rules Concerning Financial Statements and Reports in Capital Markets, it is expressed that *accounting policies should be implemented consistently; in case of changes in standards or legal regulations, these changes should be explained with their reasons.*

According to consistency standard, auditor should state in his/her report whether accounting principles implemented in the preceding period were compatible with those implemented in the account period subjected to an external audit. Consistency notion is important in the aspect of comparison of audited company's financial statements. When CMB's arrangements are examined, we see that consistency of accounting principles in financial statements issue is touched upon. Consequently, we can say that CMB's arrangements are coherent with Standard.

There is no arrangement concerning this standard stipulated in certified public accountancy and sworn in certified public accountancy legislation.

In banking legislation, there is not detailed arrangement concerning the standard of consistency. In the 32nd Article of Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks, it is expressed that *an external auditor shall verify that accounting policies implemented in the preceding period were compatible with those implemented in the account period subjected to an external audit.*

Additionally according to the 48th Article of the Regulation, *one of the stipulations to state unqualified opinion is the existence of consistency in implemented accounting policies.*

Even though there are not many arrangements concerning this Standard in banking legislation, explanations are in the same path with the Standard.

3.5.3 Standard of Adequate Disclosures

Financial statements are considered to present to different users, primarily creditors and owners, the information relevant to economic decisions they are making. For the decision makers, this information must be well timed, complete, valid and objective. Auditors have not knowledge about who the users may be or what type of decisions they may be making. The financial statements are designed to give information of a rather general nature to address as many users as possible. Auditor searches whether financial statements fulfill their duties or not by examining the disclosures which should take place in financial statements. In case of insufficient explanation, auditor states the situation in his/her report (Başpınar, 2005: 58)

The concept of adequate disclosures not only contains what information is presented but also how it is presented. The arrangement of information on the financial statements, the classification and captions used, and the terminology selected are all part of disclosure. This information, like the main portion of the financial statements, is a presentation of management. If the auditor helps the client in writing the footnotes, care should be taken to couch them in terms management would use and not in terms showing they were prepared by an auditor. In making disclosures, an auditor should remember that excessive information does not necessarily provide full disclosure. (Cook and Winkle, 1988: 48)

In certain conditions, company management may wish to prevent some information to be added to financial statements on account of the fact that they are confidential. In case of a disagreement between auditor and company management in this issue, problem should be solved by full explanation. If still client company resists to declare these information, auditor should state the situation in his/her report and give a qualified opinion (Güredin, 1997: 35).

3.5.3.1 Comparison of the Independent External Auditing within Turkey with the GAAS

In CMB legislation, regulations concerning the standard of adequate disclosure are placed in Communiqué on the Independent Audit Standards in Capital Market. According to the 5th Article of Part 30 of the Communiqué, *in case of existence of a disagreement about the efficiency of financial statement explanations, independent auditor may not declare unqualified opinion if the effect of problem is important for financial statements.*

In the Article 12, Part 34 of said Communiqué, it is specified *that if information, which is necessary to inform public sufficiently and accurately, do not take place in interim period of financial statements, independent auditor includes an explanatory paragraph in his report and declares qualified result.*

As in Standard, it is expressed in CMB arrangements as well that information given in statements should be at sufficient level for financial statement users to understand the effects of important operations and events; however if the information given in statements is considered insufficient, this would be stated in report. In this context, we can say that CMB's regulations are coherent with the Standard.

There is not any arrangement concerning this standard in certified public accountancy and sworn in certified public accountancy legislation.

In banking legislation, regulations concerning standard of adequate disclosure take place in Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks. In the 32nd Article of Regulation, it is stated that *"independent auditor should consider whether necessary correction records and/or necessary explanations in footnotes are made or not."*

According to Article 48 of the Regulation, *information in financial statements should be sufficiently clear for auditor to give unqualified opinion.*

Also in banking legislation, explanation concerning this standard is in narrow scope, but essentially, it complies with the Standard.

3.5.4 Standard of Auditor's Opinion

The fourth standard of reporting requires that the auditor must either express an opinion on the financial statements taken as a whole, including the related notes, or disclaim an opinion on those financial statements. The fourth standard gives the auditor the four options in reporting; an unqualified opinion, a qualified opinion, an adverse opinion, or disclaim of opinion. (Guy et al., 1999: 26)

Unqualified opinion is given when the financial statements are fairly presented in accordance with generally accepted accounting principles. In a qualified opinion, the auditor reports that the financial statements are fairly presented except for some material items. For example, auditor may give qualified opinion when he was unable to observe inventories. (Guy et al., 1999: 12)

In an adverse opinion, the auditor gives an opinion that the financial statements are not fairly presented in conformity with generally accepted accounting principles. Since an auditor is giving an opinion, though a negative one, sufficient evidence should exist to support this conclusion. In cases of insufficient knowledge, auditor may issue a disclaimer of opinion. (Cook and Winkle, 1988: 49)

3.5.4.1 Comparison of the Independent External Audit within Turkey with the GAAS

In CMB's arrangements, explanation concerning auditor's opinion standard is widely covered. In the 29th Part of Board's Communiqué on the Independent Audit Standards in Capital Markets, the process of the formation of audit opinion is explained. The 30th Part of Communiqué covers the reporting principles of qualified opinion, adverse opinion and disclaimer of opinion in independent audit report.

As is known, aim of independent audit is to provide an independent audit opinion whether financial statements are prepared in conformity with financial reporting standards. *In this context,* ***unqualified opinion*** *is declared when financial statements are fairly presented in accordance with financial reporting standards.* (Communiqué on the Independent Audit Standards in Capital Markets, Part 29, Article 3)

Qualified opinion is declared *when independent auditor cannot declare unqualified opinion but decides that any disagreement with management or effect of fieldwork limitation is not important and widespread enough to declare adverse opinion or disclaim of opinion.* (Communiqué on the Independent Audit Standards in Capital Markets, Part 30; Article 5)

According to the 5th Article of 30th Part of Communiqué; *in case of the probable effect of fieldwork limitation is so important and widespread that independent auditor can not obtain appropriate independent audit evidence and declare any opinion, auditor* **avoids declaring opinion.**

According to the same Article, **adverse opinion** *is declared when disagreement with management in financial statements is important and widespread and auditor considers that qualified opinion is not enough to explain the misleading and deficient structure of statements.*

Like in the Standard, according to CMB's Communiqué, auditors declare unqualified, qualified or adverse opinions or avoid declaring opinion at the end of audit. In CMB's arrangements, in which situations what sort of opinions should be declared is explained in detail. As is seen, CMB's arrangements comply with auditor's opinion standard.

58th and 59th Articles of Working Regulation pertain to the auditor's opinion standard. The 58th Article sets forth the parts of audit report and their content. As per Article 59 of the Regulation, the types of reports are as follows:

Unqualified report *is the report that includes the unqualified opinion of profession member at the end of audit activity.*

Qualified audit report *is the report that includes the limitations in audit scope which profession member met during auditing.*

Adverse report *is the report prepared by profession member with the conclusion that examined places and institutions during audit did not reflect the real situation.*

Explanations concerning auditor opinion can be found in certified public accountancy and sworn in certified public accountancy legislation, however these explanations are insufficient. It is not regulated in detail what sort of report would be given in which situations. Besides, disclaimer of opinion is not specified in the Regulation, although it is given place in the Standard. Consequently, we cannot say that arrangements in the certified public accountancy and sworn in certified public accountancy legislation comply with the Standard exactly.

In banking legislation, arrangements concerning auditor opinion standard are made in Regulation on Authorization and Activities of Institutions to Perform External Audit in Banks. The 48th Article of mentioned Regulation sets forth the situations in which unqualified opinion would be declared.

Auditor gives unqualified opinion if:

1) The external audit has been performed in accordance with the general audit principles,
2) Financial statements of the bank comply with the regulations related to accounting put into force in accordance with the Articles 37 and 38 of the Law;
3) There is coherence in accounting policies implemented;
4) Information given in the financial statements are clear enough;
5) There is no uncertainty that may affect the financial statements;
6) No restriction was encountered during the audit process.

49th Article of the Regulation sets forth the situations in which qualified or adverse opinion would be declared. Accordingly;

A senior auditor shall give ***a qualified opinion*** *if he cannot give an unqualified opinion, but the effect of the factors leading to that decision are not so important as giving a adverse opinion or disclaim to give any opinion.*

Auditor shall give ***adverse opinion*** *when there is difference of opinion with the bank management over the financial statements subjected to external audit due to inconsistencies to the regulations put into force pursuant to the Articles 37 and 38 on accounting, failure to abide by full disclosure principle and making unacceptable amendments to accounting policies; or it is concluded that the qualified opinion does not appropriately explain the insufficiency and error.*

According to said Article, the responsible partner senior auditor shall give a qualified or adverse opinion by taking into account of the opinions of the external audit team reporting to him if:

a) Information and documents related to the financial statements could not be obtained due to the existence of any issue restricting the external audit, although it is not so important as to avoid giving an opinion;

b) It is evident that the financial statements being audited could be subject to significant changes in the future by taking into account of events giving rise to doubts or the nature of transactions included in accounting records;

c) The financial statements have not been drawn up in accordance with the regulations related to accounting which have been put into force in accordance with the Articles 37 and 38 of the Law and accounting policies determined by the bank;

d) There is a disagreement with the bank with regard to errors and abuses in the items of the financial statements and how their effects should be eliminated.

According to Article 50 of the mentioned Regulation, *the responsible partner senior auditor may* ***avoid to give an opinion*** *about the financial statements if uncertainties and restrictions encountered during an external audit are significant and prevent the external auditor from giving an unqualified, qualified, or adverse opinion, sufficient evidence about a major item in the financial statements cannot be gathered, and there is not an efficient accounting and internal control system.*

Regulations in banking legislation comply with the standard of auditor's opinion. As such in the Standard, there are four types of opinions provided for in the banking legislation as well and which opinion would be declared in which situations is stated comprehensively.

Finally, it is concluded that arrangements regarding independent external audit in Turkey within the capital markets legislation largely comply with GAASs, while those within the banking legislation are in line with GAASs, though not as much as CMB's arrangements. However, arrangements made within the scope of the certified public accountancy and sworn-in certified public accountancy legislation are far from meeting GAASs.

CONCLUSION

Audit, stemming from the need for reliable information, goes back two thousand years in history. Audit practices in commercial field, the development of which lasts for thousands of years, started with Industrial Revolution in the late 18th century. In 1900s, the audit on financial statements came to the forefront with the increase in parties associated with companies; not only corruption but also the errors in transactions shown in financial statements were started to be audited. In the midst of the 20th century, internal control systems of companies gained importance in the audit, and sampling method took the place of one by one document examination. At the end of the century, a new audit approach predominated and use of statistical methods and computers became widespread. Audit scandals experienced lately have led to emerge of risk-based audit approach.

In such developed countries as Britain and USA, modern audit studies were launched in the 19th century. Auditing standards, the indispensable of a qualified audit, for the first time issued in 1947 in the U.S. by AICPA under the name of "Generally Accepted Auditing Standards-GAAS". GAASs are the minimum criteria that must be followed in order to be able to conduct an audit of high quality. These standards have undergone very few changes and still remain valid.

In Turkey, comprehensive studies oriented towards implementation related to auditing standards were conducted by CMB forty years after issuance of GAASs. Several provisions of the Regulations on Working and Certifications, which were issued based on the Law No: 3568, are also in the nature of auditing standards. However, as these standards are not at the same level as GAASs, first TMÜDESK and afterwards TÜDESK were established by TÜRMOB. International auditing standards were translated into Turkish by TÜDESK; however, no progress has achieved in the development of national auditing standards.

As known, studies on independent external audit in Turkey have been carried out within the scope of capital market, certified public accountancy and sworn-in certified public accountancy and banking legislations. This study, surveys to what extent the independent external audit performed within these legislations complies with GAASs, the minimum standards required to be followed during audit.

Following the study, it is concluded that arrangements made within the scope of capital markets legislation are in parallel with “General Standards” and “Fieldwork Standards” of GAASs. As for “Reporting Standards”, there are several differences detected. For instance, according to the Standard of Generally Accepted Accounting Principles, the financial statements should be checked for compliance with generally accepted accounting principles, while the arrangements of CMB indicate that they are required to be checked for compliance with financial reporting standards. However, as is mentioned before, this discrepancy will be removed with the efforts for eliminating the differences between GAAP and IFRS. It is furthermore seen that arrangements made in capital market legislation with regard to other three reporting standards are in parallel with GAASs.

Arrangements regarding independent external audit in the legislation of certified public accountancy and sworn-in certified public accountancy are detected to be compliant with the “Technical Training and Proficiency Standard”; except for the lack of arrangement with respect to continuation of professional training, which is envisaged in the Standard. There are arrangements regarding “Standard of Independence in Mental Attitude”; yet, they include neither comprehensive arrangements directed towards practice nor the situations that can damage independence. Besides, no arrangement has been made in parallel with Sarbanes-Oxley Act. As for the third standard of General Standards, “Due Professional Care Standard” arrangements made in the legislation of certified public accountancy and sworn-in certified public accountancy show differences. Due Professional care is defined as a behavior pattern of an auditor to guarantee his/her independence rather than one that needs to be shown at each phase of the audit study, as indicated in the Standard.

When considered the arrangements made within the scope of certified public accountancy and sworn-in certified public accountancy from the point of "Fieldwork Standards"; it is seen that there are arrangements that comply with "Planning and Supervision Standard"; however there is none concerning "Internal Control Standard" at a level comparable to GAASs. On the other hand, arrangements with respect to "Standard of Sufficient Competent Evidential Matter" in this legislation are in line with GAASs.

It was further found out that the legislation of certified public accountancy and sworn-in certified public accountancy does not cover any arrangement concerning Generally Accepted Accounting Principles, Consistency and Adequate Disclosure Standards among reporting standards excluding those on" Auditor's Opinion Standard". Yet, these are not at a sufficient level.

In the banking legislation, there are no arrangements on "Technical Training and Proficiency Standard"; however, reference is made to Law No: 3568. Concerning "Standard of Independence in Mental Attitude", arrangements are satisfactory; however, there is not enough arrangement on "Due Professional Care Standard".

In general, arrangements regarding "Fieldwork Standards" in the banking legislation comply with GAASs. Only it covers none with respect to supervision part of "Planning and Supervision Standard".

With respect to "Standard of Generally Accepted Accounting Principles", which is one of the reporting standards, arrangements in banking legislation differ from those in GAASs. According to the Standard of Generally Accepted Accounting Principles, the financial statements should be checked for compliance with generally accepted accounting principles while the arrangements in banking legislation, as in the case of CMB, indicate that they are required to be checked for compliance with financial reporting standards. This discrepancy will also be removed with the efforts for eliminating the differences between GAAP and IFRS. It was seen that arrangements regarding other three Reporting Standards are in line with GAASs.

Ultimately, it is concluded that arrangements regarding independent external audit in Turkey within the capital markets legislation comply with GAASs, while those within the banking legislation are in parallel with GAASs, though not as much as CMB's arrangements. It is further detected that arrangements made within the frame of the certified public accountancy and sworn-in certified public accountancy legislation, regulating the accountancy and auditing profession in Turkey, are far from meeting GAASs, the minimum standards in audit.

One of the biggest obstacles in front of the independent external audit in Turkey is the existence of different arrangements within different legislations. Therefore, the draft law on "Turkish Auditing Standards and Public Oversight Agency" should be passed immediately; establishment of a professional association that is to set national auditing standards in line with international auditing standards as well as implementation of auditing standards by single authority should be ensured.

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