

**SYLLABUS****B.Com - III Year****Subject – Auditing**

UNIT – I	Introduction: Meaning and Nature of Auditing Objectives. Limitations, Classification of Audit, Errors and Frauds, Code of Conduct & value System for Auditors Audit Plan & Program
UNIT-II	Internal Control and Internal Check: Meaning and objectives, Features of a good Internal Control system. Internal Control Questionnaire, Checklist, Text. Internal Audit, Test checking, Audit Sampling
UNIT-III	Vouching and Verification: Vouching - Meaning and Objective Verification - Assets and Liabilities
UNIT-IV	Audit of Companies: Audit of company under Company Act 2013, Appointment, Remuneration of Auditor, Rights & Duties of auditor, Auditor's report.
UNIT-V	Special Areas of Audit: Cost Audit, Tax Audit, management Audit, Performance Audit, Social Audit, Environmental Audit, Audit of Banking & Insurance Company, Audit of Educational Institute, Club & Charitable Organisation.



UNIT-I

INTRODUCTION

Meaning of Auditing - According to AAS-1 An audit is an independent examination of financial information, of any entity, whether profit oriented or not, and irrespective of its size or legal form, when such an examination is conducted with a view to, expressing an opinion thereon.

The person conducting audit is known as the auditor, he makes a report to the person appointing him after due examination of the accounting records and the accounting statement in the form of an opinion on the financial statements. The opinion that he is called upon to express is whether the financial statement reflects a true and fair view.

A complete and comprehensive definition : “Auditing is a critical examination of the books of accounts of an organization, which is conducted by an independent individual skillfully on the basis of vouchers and other information, with an object to reporting that the profit and loss account prepared for a certain period expresses the true and fair profit or loss of the organization and the balance sheet of the organization, prepared on a certain date, depicts a true and fair picture of the financial position of the organization on the particular day”.

Definition:

R.B. Bose : “Audit may be said to be the verification of the accuracy and correctness of the books of accounts by an independent person qualified for the job and not in any way connected with the preparation of such accounts.

Advantages of an Audit:

- (a) Safeguards the financial interest of persons who are not under management of the entity, i.e., partners or shareholders.
- (b) Acts as a moral check on the employees from committing frauds and errors.
- (c) Helpful in setting liability for taxes, negotiating loans and determining the purchase consideration for a business.
- (d) Useful for settling trade disputes whether it is a matter of performance bonus or increment or it is claim for the damages due to fire or other accident.
- (e) Discover the areas of wastages and losses occurring due to the absence or inadequacy of internal checks or internal control measures.



- (f) Audit report generally state the fact that whether proper books of account and related records have been properly kept so as to make the deficiencies or inadequacies good in this respect.
- (g) As an appraisal function, audit reviews the existence effectiveness and continuity of various controls in the organizations and reports weaknesses, inadequacies, etc., in them.
- (h) Audited accounts are of great help in the settlement of accounts at the time of admission or dissolution or death or retirement of partner.

The objectives of audit:

- 1. Examination of the Truth and Fairness of Final Accounts :
- 2. Discovery of Errors :
- 3. Detection of Fraud :
- 4. Prevention of Frauds and Errors :
- 5. Advice to Management :
- 6. Ascertaining true Financial Position of Business :
- 7. Objectives determined by International Auditing Practices Committee :

Types of Audit:

- (1) On the basis of need of audit
 - a. External Need b. Internal Need
- (2) On the basis of period of audit
 - (a) Continuous Audit (b) Interim Audit (c) Final/Annual Audit

1. On the basis of Need:

- a. The auditor appointed to satisfy the internal or managerial needs of the organization is known as INTERNAL AUDITOR. According to AAS-7 The internal audit function constitutes a separate component of internal control established with the objective of determining whether other internal controls are well designed and properly operated.
- b. The auditor appointed to satisfy the External Needs of the organization is known as EXTERNAL AUDITOR.
- c. If external need is a statutory need the same external auditor is known as STATUTORY AUDITOR. For example :



2. On the basis of Period of Audit:

A. Continuous audit - A continuous audit is one where the auditor or his staff is constantly engaged in checking the accounts during the whole period or where the auditor or his staff attends at regular or irregular intervals during the period.

The following features of continuous audit come to light on analysis of the above definition.

- (a) It is carried throughout the year.
- (b) It is conducted at regular or irregular intervals depending on auditors professional judgment.
- (c) The accounts are taken for scrutiny as and when prepared.
- (d) Final accounts i.e. trial balance, profit and loss account and balance sheet are audited at the end of the year.

Advantages of Continuous Audit:

- (i) Exhaustive and intensive.
- (ii) Greater possibility of exposure of errors and frauds.
- (iii) Early detection of errors & Frauds.
- (iv) Moral impact on employees.
- (v) Quick preparation of final accounts.
- (vi) Early planning for future.
- (vii) Proper advice of auditor
- (viii) Early rectifications of errors.
- (ix) Facility for interim accounts.

Disadvantages of Continuous Audit:

- (i) Possibility of change in audited accounts.
- (ii) Snags in routine work.
- (iii) Adverse moral impact
- (iv) More expensive
- (v) Dislocation of sequence of work.
- (vi) Mechanization of work
- (vii) Sloth in work.

B. Annual Audit : Annual audit is one which is carried out only at the end of an accounting period, spicer and pegler have defined it as. An audit which is not



commenced until after end of the financial period and is then carried on until completed. Annual audit is also called periodical, final or completed audit.

Characteristics: The main Characteristics of annual audit are as follows :

- (a) It is done at the close of the financial year books of account have been closed and final accounts drawn by the management of the entity.
- (b) The audit work is completed at a stretch i.e. in a single continuous session.
- (c) Generally this type of audit suitable to small organizations.

C. Interim Audit : An audit conducted between two annual audits is called interim audit. More commonly it is known in case of banks as half yearly review. Interim audit helps management to take timely and appropriate decisions for example declaration of interim dividend or valuation of shares to decide swap ratio in case of a merger. Interim audit is gaining statutory status now a days various regulating authorities like SEBI and RBI requires periodic audited financial statements in between the to annual audited financial statements. However, it is generally carried out by professionally qualified auditors.

Limitations of Audit

- 1. Auditing does not guarantee 100% correctness.
- 2. All frauds are not necessarily disclosed by audit.
- 3. The auditor expresses only his opinion.
- 4. Auditing is not a credential of the perfect honesty of employees.
- 5. Auditing does not certify the commercial prudence of transactions.
- 6. Auditing does not pay attentions to trivial.
- 7. Auditing is not supported by practical independence.

❖ Audit Process:

The steps in audit process is :

- 1. Appointment of auditor
- 2. Determination of Objective and Scope of audit
- 3. Obtaining Knowledge of Clients business
- 4. Evaluating accounting system, Internal control and Audit risk.



5. Audit Planning and programming, Determining the nature timing and extent of audit procedure and co-ordination of work.
6. Collection of audit evidence
7. Drawing conclusions and making report.

❖ Preparation of Audit Programme:

Audit programme is a description, memorandum or outline of the work to be done in an audit and often of the time allotted and personnel assignments, prepared by a Principal as a definition of audit scope, or by an auditor for the guidance and control of assistants. It is the auditors plan of action, specifying the procedures to be followed.

Objects of audit programme :

- a. To obtain informations regarding the accounting system, policies and control techniques of the client.
- b. To ascertain the extent to which internal control techniques can be banked upon.
- c. To lay down the nature, time and extent of audit techniques to be adopted.
- d. To co-ordinate the total work.

Characteristics of good audit programme

- i. Explicit and clarity of expression.
- ii. Segmentation of work in the light of different aspects of accounting.
- iii. Logical flow of accounting documents
- iv. Elasticity
- v. Review of work
- vi. According to scope of audit
- vii. Based on evidences
- viii. Record of movements and accomplishments.

Advantages of audit programme :

- i. Division of work as per ability
- ii. Determination of responsibilities
- iii. Progress of work

Disadvantages :

- i. Mechanisation of work
- ii. No motivation for free decision
- iii. Want of constructive thinking



- iv. Change of employees won't affect work
- v. Uniformity in work
- vi. Protection in court of law
- vii. Complete examination
- viii. Time saver
- ix Facility of review
- x. Pursuance of audit principles
- iv. Want of moral influence
- v. Planned frauds are undisclosed
- vi. Disabilities remain concealed
- vii. Plea against auditor

❖ Audit working papers:

Audit working papers are personal written materials which an Auditor prepares with regard to all audits and contains techniques adopted by the auditors, his decisions and conclusions and relevant information regarding financial statements.

Some papers included in Audit Working Papers;-

1. The agreement regarding the appointment if the auditor or letter of appointment
2. Technical Features of the audited business.
3. Audit Programme
4. Certificates of officials in regard to such important matters as bad debts, valuation of stock, unpaid expenses, accrued income etc
5. Certificate issued by the banks in regard to the bank balance of the client certain date, safe custody of documents etc.
6. Correspondence between the auditor and the debtors, creditors, etc. the client.
7. Rough trial balance.
8. Important extracts from the minute books
9. Particulars of investment.
10. Draft final accounts.
11. A copy of the auditors book.

Objects of keeping Audit-Working Papers;-

1. Certification of the correctness of record and report
2. Use as references, during discussion with the employer.



3. Defensive position of the auditor in case of legal dispute and court proceedings.
4. Guide for Subsequent examinations.
5. To co-ordinate and organize the work of audit clerks.

Ownership of Audit-Working Papers :-

These are the property of the auditor, whether prepared by him or presented to him by the owner of the business and therefore must be kept in safe custody.

Filing of Audit-Working Papers is a necessity. The auditor keeps these papers for his defense, reference, future guidance and as a proof of his. According to section 209 of the Indian Companies Act 1956, the books of accounts of a company must be kept safe up to 8 years after the relevant year.

❖ Audit Note Book:-

An important component of Audit-Working papers is audit note- book basically maintained by the audit clerk in which he notes down the important points and enquires which he has to refer to officials clients or to discuss with his senior or the auditor himself.

Contents of audit note book:

1. Technical details about the business.
2. Queries for which explanations and information have to be demanded.
3. Missing vouchers and invoices whose duplicates have to be obtained.
4. Fraud and errors found in the books during the course of audit.
5. Details to be included in audit report.
6. Notes regarding system of maintaining accounts.
7. Information to be needed in future.
8. Names of officials who certify bad debts, depreciation, etc.
9. Record of all important correspondence.
10. Total of important ledger accounts.
11. Progress of audit work.
12. Record of suggestions made by the audit staff.



Advantages:-

1. Defense in court of law.
2. Yard-stick of the efficiency and diligence and skill of the auditor,
3. Guide for future.
4. Future references,
5. Permanent certificate of audit.