

AUDITING

Dr Shubhangee L Diwe
Dept of Commerce
Baliram patil college Kinwat)

UNIT:1 Introduction to Auditing

- ▶ The term audit is derived from the Latin term “Audire” which means to hear. In early days an auditor used to listen to the accounts read over by an accountant in order to check them. The original objective of auditing was to detect and prevent errors and frauds.
- ▶ In Indian the Companies Act 1913 made audit of company accounts compulsory.
- ▶ “Auditing is such an examination of the books, accounts, and vouchers of a business shall enable the auditor to satisfy himself whether or not the balance sheet is properly drawn up so as to exhibit a true and correct view of the state of affairs of the business according to his best of the information given to him and as shown by the books”. SPICER AND PEGLAR
- ▶ “Auditing is the examination of the books and records of a business in order to ascertain or verify and report up on the facts regarding the financial operations and the results thereof”.

Origin and Evolution of Auditing

- ▶ In early days an auditor used to listen to the accounts read by an accountant in order to check them. Auditing is as old as accounting.
- ▶ Auditing evolved and grew rapidly after the industrial revolution in the 18th century. This was with the growth of the joint stock companies the ownership and management became separate.
- ▶ The shareholders needed a report from an independent expert on the accounts of the company audit was expected to ascertain whether the accounts were true and fair rather than detection of errors and frauds.
- ▶ In India the Companies Act ,1913 made audit of company accounts compulsory with the increase in the size of companies and the volume of transactions. The companies Act,1913 also prescribed for the first time qualifications of auditor.
- ▶ The IASC and ASB of the institute of chartered accountants of India have developed standards of accounting and auditing practices.
- ▶ Thus auditing has come a long way from hearing of accounts to taking the help of computers to examine computerized accounts.

Scope of Auditing

- ▶ Legal requirements
- ▶ Entity aspects
- ▶ Reliable Information
- ▶ Proper Communication
- ▶ Evaluation
- ▶ Test
- ▶ Evidence

Features of Auditing

- ▶ Systematic and Scientific Examination
- ▶ Done by qualified person/group
- ▶ Shows the financial position
- ▶ Review of internal control
- ▶ Require evidences
- ▶ Require authentication
- ▶ Require thorough examination

Objectives of Auditing

- ▶ Auditors are basically concerned with verifying whether the accounts exhibit true and fair view of the business. The objectives of auditing depends upon the purpose of his appointment.

Primary objectives:

- ▶ The primary objective of an auditor is to respect to the owners of the business expressing his opinion whether account exhibits true and fair view of the state of affairs of the business.
- ▶ The auditor is also concerned with verifying how far the accounting system is successful in correctly recording transactions.
- ▶ An Auditor must examine the internal control and internal check.
- ▶ Auditor must verify whether proper accounting principles and procedures are followed.
- ▶ Auditor must verify whether all books of accounts as required by law are kept.
- ▶ Auditor verify the authenticity and validity of the transactions.

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Secondary Objectives:

- ▶ Detection and prevention of errors
 - Errors of Omission
 - Errors of Commission
 - Errors of Compensation
 - Errors of principle
- ▶ Detection and prevention of frauds
 - Misappropriation of cash
 - Misappropriation of Goods
 - Manipulation of Accounts

Advantages of Auditing

- ▶ Verification of books and statements
- ▶ Discover and prevention of errors
- ▶ Discover and prevention of fraud
- ▶ Independent opinion
- ▶ Protects the interest of shareholders
- ▶ Proper supervision
- ▶ Disputes settlement
- ▶ Information about Economic condition
- ▶ Advantage for General public

Limitations/disadvantages of Auditing

- ▶ Non detection of errors/ frauds
- ▶ Dependence on explanation by others
- ▶ Dependence on opinion of others
- ▶ Corrupt practices to influence the auditor
- ▶ No assurance difficult to verify certain items
- ▶ Effect of inflation
- ▶ Conflicts with others

Types of Auditing

Classification on the basis of ownership:

- ▶ Proprietorship Audit
- ▶ Partnership Audit
- ▶ Companies Audit
- ▶ Trusts Audit
- ▶ Cooperative societies
- ▶ Government Departments

Classification on the basis of time:

- ▶ Interim Audit
- ▶ Final Audit

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- ▶ Continuous audit
- ▶ Balance Sheet Audit

Classification on the basis of objectives:

- ▶ Independent audit
- ▶ Financial audit
- ▶ Internal audit
- ▶ Cost audit
- ▶ Tax audit
- ▶ Government audit
- ▶ Secretarial audit

Standards of Auditing(SA)

- ▶ SA 200: Basics Principles Governing An Audit
- ▶ SA 210: Terms Of Audit Engagement
- ▶ SA 220: Quality Control For Audit Work
- ▶ SA 230: Audit Documentation
- ▶ SA 240: The Auditor Responsibilities Relating To Fraud
- ▶ SA 250: Consideration Of Laws And Regulation In An Audit Of Financial Statement
- ▶ SA 260: Communication With Those Charged With Governance
- ▶ SA 265: Communication Deficiencies In Internal Control To Those Charge With Governance
- ▶ SA 299: Responsibilities Of Joint Director
- ▶ SA 300: Planning Of Audit Of Financial Statement

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- ▶ SA 315: Understanding The Entity And Its Environment And Assessing The Risk Of Material Misstatement
- ▶ SA 320: Audit Materiality
- ▶ SA 330: The Auditor Responses To Assessed Risks
- ▶ SA 402: Audit Considerations Relation To Entities Using Service Organizations
- ▶ SA 450: Evaluation Of Misstatement Identified During The Audit
- ▶ SA 500: Audit Evidence
- ▶ SA 510: Audit Evidence- Additional Consideration For Specific Items
- ▶ SA 505: External Confirmations
- ▶ SA 510: Initial Audit Engagement

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- ▶ SA 520: Analytical Procedures
- ▶ SA 530: Audit Sampling
- ▶ SA 540: Auditing Accounting Estimates
- ▶ SA 550: Related Parties
- ▶ SA 560: Subsequent Events
- ▶ SA 570: Going Concern
- ▶ SA 580: Written Representations
- ▶ SA 600: Using The Work Of Another Auditor
- ▶ SA 610: Relying Upon The Work Of An Internal Auditor
- ▶ SA 620: Using The Work Of An Expert

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- ▶ SA 700: The Auditor's Report On Financial Statement
- ▶ SA 705: Modifications To The Opinion In The Independent Auditor's Report
- ▶ SA 706: Emphasis Of Matters Paragraphs And Other Matter In The Independent Auditor's Report
- ▶ SA 710: Comparatives Information
- ▶ SA 720: The Auditor Responsibility In Relation To Other Information In Documents Containing Audited Financial Statement

Auditing and assurance standard Board- ICAI

- ▶ The international auditing and assurance standards board (IAASB) was founded in March 1978. It was previously known as the international auditing practices committee (IAPC).
- ▶ The IAASB is an independent standard setting body that serves the public interest by setting international standards for auditing, quality control, review other assurance and related services and by facilitating the convergence of international and national standards. Auditing and assurance standard board of the institute formulates the auditing standards.
- ▶ ICAI constituted the Auditing Practices Committee (APC) on September 17, 1982 to spearhead the new framework of statements on standard auditing practices (SAPs) and guidance notes (GNs) inter alia to replace various chapters of the old omnibus statement on Auditing Practices issued in 1964.
- ▶ In July, 2002 the auditing practice committee has been converted into an auditing and assurance standards board by the council of the institute to be in line with the international trend.

Objectives of Auditing and Assurance Standard Board

- ▶ To review the existing and emerging auditing practices worldwide and identify areas in which standards on quality control engagement standards and statements on auditing need to be developed.
- ▶ To formulate engagement standards, standards on quality control and statements on auditing so that these may be issued under the authority of the council of the institute.
- ▶ To review the existing standards and statements on auditing to assess their relevance in the changed conditions and to undertake their revision, if necessary.
- ▶ To develop Guidance notes on issues arising out of any standard, auditing issues pertaining to any specific industry or on generic issues, so that those may be issued under the authority of the council of the institute.
- ▶ To review the existing guidance notes to assess their relevance in the charged circumstances and to undertake their revision, if necessary.
- ▶ To formulate and issue technical guides, practice manuals, studies and other papers under its own authority for guidance of professional accountants in the cases felt appropriate by the board.

Procedure for issue of standards by AASB

The auditing and assurance standards board of the institute(AASB) formulates the auditing standards. Broadly following is the procedure for formulating auditing standards.

- ▶ The auditing and assurance standards board identifies the areas where auditing standards need to be formulated and the priority in regard to their selection.
- ▶ In the preparation of the auditing standards, the board is normally, assisted by study groups comprising of a cross section of members of the institute.
- ▶ On the basis of the work of the study groups, an exposure draft of the proposed auditing standard is prepared by the board and issued for comments of the members.
- ▶ After taking into the comments received, the draft of the proposed auditing standard is finalised by the board and submitted to the council of the institute.
- ▶ The council considers the final draft of the proposed auditing standard and, if necessary, modifies the same in consultation with the board. The auditing standard is then issued under the authority of the council.