

## Chapter 1 - Nature, Objective and Scope of Audit

- Topics to be Covered:
- (i) Meaning, Nature, Objective and Scope of Audit
  - (ii) Inherent limitations of Audit
  - (iii) Meaning, Nature and Types of Engagements
  - (iv) Qualities of Auditor
  - (v) Engagement and Quality Control Standards (EQCS)

### (i) Meaning, Nature, Objective and Scope of Audit:

(a) Meaning of Auditing: Audit may be defined as:

"Independent Examination of financial information of an entity, whether profit making or not; and irrespective of its size or form, when such examination is conducted so as to express an opinion on true and fair view of financial position and financial performance."

### Points to be ensured that F.S. not misled anyone:

- (i) Ensure that accounts are drawn up with reference to entries in books of Account. (Posting)
- (ii) Entries in books of accounts are supported by sufficient and appropriate Evidences. (Vouchers)
- (iii) None of entries in books of account has been Omitted. (Omission | <sup>No</sup>Completeness)
- (iv) Information contained in F.S. is clear and unambiguous. (Understandable)
- (v) Amount shown in F.S. are properly classified, described and disclosures are made in conformity with applicable ASs. (Classification, Presentation)
- (vi) F.S. reflects true and fair view of financial results and financial position.

## (B) Interdisciplinary Nature of Auditing:

- (i) Auditing and Accounting: Auditing begins when accounting ends. Auditor must have sound knowledge of Accounting Principles, Accounting Standards etc.
- (ii) Auditing and Law: While carrying out audit, Auditor is required to ensure compliance of applicable laws that affects the determination of amount and disclosures in the financial statements. Hence auditor must have sound knowledge of Business, Corporate, taxation and other laws.
- (iii) Auditing and Economics: Auditor must have sound knowledge of Economics so as to understand the economic environment in which the client operates.
- (iv) Auditing and Statistics: While carrying out audit, Auditor is required to determine and select the samples to be examined. For this purpose, statistical techniques helps the Auditor a lot.
- (v) Auditing and Behavioural Sciences: During audit, Auditor interacts with many persons within and outside the Entity client; hence he must be able to understand their conduct and behaviour.
- (vi) Auditing and Financial Management:  
Auditor deals with the financial statements which includes financial figures; hence Auditor must have knowledge of financial management aspects like fund management, inventory management, etc.

(C) Objectives of Audit as per SA 200: - Covered in Introductory Lecture —

(D) Scope of Audit:

(i) Elements to be included in Scope of Audit:

(a) Ensure that scope of audit covers all aspects of Entity related with F.S.

(b) Ensure that information contained in accounting records is reliable and sufficient.

(c) Study and Evaluate Accounting system and related Internal controls.

(d) Ensure that information is properly disclosed in the financial statements as per statutory requirements.

(e) Ensure that F.S. properly summarise the events and transactions recorded therein.

(f) Evaluate whether accounting policies selected by management are proper and whether such policies are consistently applied period to period basis.

(ii) Elements not included in scope of audit:

(a) Areas which fall outside the domain of his competence  
For Ex: Future Projections;  
Non-financial matters;  
Business Viability etc.

(b) Authentication of documents  
(As auditor may not have relevant expertise).

### Summary

- ① All aspects related with F.S.
- ② Reliability / Sufficiency of Info.
- ③ Accounting system and I.C.
- ④ Disclosures given in F.S.
- ⑤ Events and transactions.
- ⑥ Accounting policies

- (E) Audit vs. Investigation: - Audit is not an official investigation into alleged wrong doings.
- Auditor does not have specific powers of search; or recording statements of witnesses on oath; or issuing summons to others, etc; which are required for carrying out an official investigation.
  - Investigation is a critical examination of records with a specific purpose that is narrow in nature.
  - Audit is independent examination so as to express an opinion on true and fair view of financial statements; hence scope of audit is general and broad.

- (F) Benefits of Audit:
- (i) Audited accounts and financial statements provide high quality information which boosts up the confidence of users.
  - (ii) Safeguards the interest of investors, not engaged in day to day activities.
  - (iii) Audit puts a moral check on employees in committing fraud.
  - (iv) Audited accounts helps the Government for determining tax liabilities.
  - (v) Audited accounts are being relied upon by Banks, lenders for their credit decisions.
  - (vi) Audit helps in detection of fraud or error or both.
  - (vii) Audit involves review of existence and operation of various controls, so that deficiencies, if any, can be rectified.

## (G) Mandatory Audit vs. Voluntary Audit:

↓  
- Audit Required under law

- For Example:

(a) Audit under Companies Act, 2013 (Sec. 143)

(b) " " Income-tax Act, 1961 (Sec. 44AB)

(c) " " LLP Act, 2008

(d) " " Banking Regulation Act, 1949

(e) " " Co-operative Societies Act, 1912

↓  
- Audit not required under any statutory requirements

- An entity may be required to get the accounts audited for the purpose of obtaining loans / Grant / Subsidies etc.

- For Ex: Schools may be required audit for obtaining Grants or assistance from Govt.

## (H) Who appoints Auditor:

(i) Non Govt. Companies → BOD; Members

(ii) Govt. Companies → C & AG of India

(iii) Partnership Firm → Partners

(iv) LLP → Designated Partners

## (I) To whom audit report is submitted: To the person who appoints the auditor.

Company → Members / Shareholders

Firm → Partners

---