

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

- Topics :
- (i) Meaning, Objective, nature 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: 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 results and financial position.

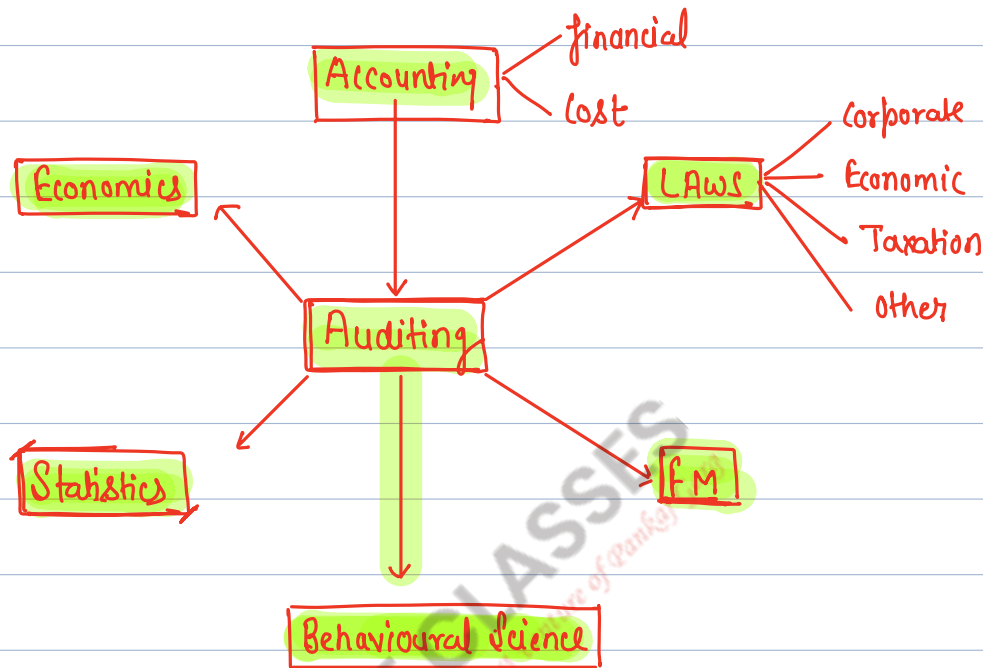
(Sttn. of Profit/loss) (Balance Sheet)

Points to be ensured that f.s. not mislead any person:

- (a) Ensure that accounts are drawn with reference to entries in books of prime entry (i.e. Ledger Posting)
- (b) Ensure that entries in books of account are supported by sufficient and appropriate evidences (i.e. Voucher)
- (c) None of the transaction is omitted to be recorded in books of A/c. (i.e. No Omission / Completeness)
- (d) Information contained in f.s. is clear and unambiguous. (i.e. Understandability)
- (e) Amount shown in f.s. are properly classified, described and disclosures as made in conformity with applicable ASs. (Classification, Presentation)

(f) f.s. reflects **true and fair view** of financial results and financial position. (true and fair view).

(B) Inter-disciplinary nature of Auditing:



(i) Auditing and accounting: Auditing begins when accounting ends.

Auditor must have sound knowledge of:

- (a) Accounting Principles;
- (b) Accounting standards etc.

(ii) Auditing and Law: - While performing audit, auditor is required to ensure compliance of applicable laws that affects the determination of amount and disclosures in the financial statement

- Hence auditor must have sound knowledge of
 - (a) Business laws ;
 - (b) Corporate and Economic Laws ;
 - (c) Taxation laws etc .

(iii) Auditing and FM: Auditor deals with the financial statements which comprises of financial figures. Hence, auditor must have knowledge of financial management aspects like:

- (a) Fund Management
- (b) Inventory Management
- (c) Trade Receivable Management etc.

(iv) Auditing and Behavioural science: While carrying out audit, auditor has to interact with many persons within and outside the Entity. Hence, auditor must be able to understand their conduct and behaviour.

(v) Auditing and Economics: Auditor is required to understand the economic environment of the Entity in which it operates. Hence auditor must have knowledge of Economics Principles to obtain the understanding of client's Economic Environment.

(vi) Auditing and Statistics: While carrying out audit, auditor is required to determine and select the samples to be examined. Samples selected on statistical techniques are considered more appropriate as compared to samples selected on judgement basis. Hence auditor must be able to apply the statistical techniques.

(c) Objectives of Audit as per SA 200: - Already discussed in Introductory lecture -

(D) Scope of Audit: Scope of audit is generally ascertained from:

- (i) Statutory provisions
- (ii) Pronouncements of ICAI (For Ex: Standards of Auditing)
- (iii) Letter of Engagement issued by Auditor.

Imp.

(i) Elements to be included in scope of audit:

- (1) Ensure that scope of audit covers all aspects of Entity related with f.s.
- (2) Ensure that information contained in accounting records is reliable and sufficient.
- (3) Study and Evaluate Accounting System and related Internal Controls.
- (4) Ensure that information is properly disclosed in the f.s. as per statutory requirements.
- (5) Ensure that f.s. properly summarise the events and transactions recorded therein.
- (6) Evaluate whether Accounting Policies selected by mgmt. are proper and whether such policies are consistently applied period to period basis.

(ii) Elements not included in scope of audit:

(1) Areas which fall outside the domain of auditor's competence.

For Ex: Future projections;
Non-financial matters;
Business Viability.

(2) Authentication of documents: As auditor may not have relevant expertise to check genuineness of documents

(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.
- Without such powers, it is not possible to carry 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 its scope is general that is broader in nature.

(F) ^{Imp}Benefits of Audit:

- (1) Audited accounts and f.s. provide high quality information which enhance the confidence of users of f.s.
- (2) Audit safeguards the interest of investors, who are not engaged in day to day activities.
- (3) Audit puts a moral check on employees from committing frauds.
- (4) Audited accounts helps the Govt. in determination of tax liabilities.
- (5) Audited accounts are being relied upon by bankers, financial institutions, lenders for their credit decisions.
- (6) Audit helps in detection of fraud or error or both.
- (7) Audit involves review of existence and operations of various controls, so that deficiencies, if any, can be rectified.

(G) Types of Audit:

(i) Mandatory Audit (Statutory Audit
External Audit)

- Audit required by statutory provisions.

- Examples:

(A) Audit under Companies Act, 2013

(B) " " Income-Tax Act, 1961

(C) " " LLP Act, 2008

(d) " " Banking Regulation Act, 1949

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

(ii) Voluntary Audit
(Non-statutory audit)

- Audit not required by statutory provisions.

- Such audit may be required to get financial assistance from bank, F.I., lenders etc.

- Such audit may also be required for obtaining grants, financial assistance from Govt., licenses etc.

(H) Who appoints Auditor:

(i) Non-Govt. Companies → BOD ; Members

(ii) Govt. Companies → C&AG of India

(iii) Partnership firm → Partners

(iv) Limited liability Partnership → Designated Partners

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

Company → Members

Firm → Partners