PRACTICAL AUDITING

E-Material

III B.Com

Compiled By

Dr.R.Dhanalakshmi

Assistant Professor in Commerce

Government Arts College, Coimbatore

Year	Subject Title	Sem.	Sub Code
2018 -19 Onwards	Skill Based Subject –III : PRACTICAL AUDITING	V	18BCO55S

Objective: To understand the subject-matter under examination and how performance will be Assessed.

UNIT – I

Definitions – Objects and Scope of Auditing – Classification of Audits – Basic Principles and Processes

UNIT – II

Audit Programme – Internal Control, Internal Check and Internal Audit – Vouching – Vouching of Cash Transactions and Trading Transactions

UNIT – III

Verification and Valuation of Assets and Liabilities – Depreciation – Provisions and Reserves

UNIT – IV

Company Audit – Appointment and Removal of Auditor – Qualification and Disqualification – Rights and Duties of Auditor – Liabilities of Auditor – Auditor's Report

UNIT – V

Audit of Public Accounts – Cost Audit – Auditing in an EDP Environment.

****

Text book :

1. Principles and Practices of Auditing – B.N. Tandon – Sulatan Chand and Sons

***Reference Books*:**

1. Principles and Practices of Auditing – Dinkar Pagare– Sulatan Chand and Sons
2. Auditing- Principles and Practice –Pradeep Kumar, Baldev Sachdeva and Jawant Singh, kalyani publishers
3. A Hand Book Of Practical Auditing - B. N. Tandon, S. Sudharsanam & S. Sundharabahu. Sulatan Chand and Sons

PRACTICAL AUDITNG
UNIT-I

Origin of Audit
The term audit is derived from the Latin term 'audire,' which means to hear. In old days whenever proprietors suspected a fraud or error, certain people were appointed to hear verbal evidence of transaction. (in barter system)

Meaning of Audit
An official inspection of an organization's accounts, typically by an independent body. "Audits can't be expected to detect every fraud" conduct an official financial inspection of (accompany or its accounts).

Definitions of Auditing
An unbiased examination and evaluation of the financial statements of an organization. It can be done internally (by employees of the organization) or Externally (by an outside firm).

Auditing refers to a systematic examination of books, accounts, documents and vouchers of an organization to ascertain how far the financial statements present a true and fair view of the concern.

"Auditing is an examination of accounting records undertaken with a view to establish whether they correctly and completely reflect The transactions to which they relate." Prof. L.R.Dicksee.4

ISA (International Standard of Auditing) "An Audit is the independent examination of financial statement or related information of an 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"

FEATURES OF AUDITING
a. Audit is a systematic and scientific examination of the books of Accounts of a business;
b. Audit is undertaken by an independent person or body of persons Who are duly qualified for the job.
c. Audit is a verification of the results shown by the profit and loss Account and the state of affairs as shown by the balance sheet.
d. Audit is a critical review of the system of accounting and internal Control.
e. Audit is done with the help of vouchers, documents,
f. Information and explanations received from the
g. Authorities.

h. f. The auditor has to satisfy himself with the authenticity
i. of the financial statements and report that they exhibit
j. a true and fair view of the state of affairs of the concern.
k. g. The auditor has to inspect, compare, check, review,
l. scrutinize the vouchers supporting the transactions
m. and examine correspondence, minute books of share
n. holders, directors, Memorandum of Association and
o. Articles of association etc., in order to establish
p. Correctness of the books of accounts.

Accounting vs Auditing

Accounting	Auditing
It's a continuous process carried out throughout the year.	It's a onetime activity after the closure of accounting year.
No prescribed qualification is required to be an accountant.	He must be the member of Institute of Chartered Accountants of Pakistan to become an auditor.
An accountant is a employee of the company.	An auditor is an independent professional.
An accountant gets regular salary for his work.	He gets remuneration for his professional work. Audit fees.
Accounting is concerned with recording of Business transactions systematically. Accounting precedes, auditing	Its concerned with verification of accounts prepared by The accountant. Auditing succeeds accounting

Difference between Accounting and Auditing

BASIS FOR COMPARISON	BOOKKEEPING	ACCOUNTING
Meaning	Bookkeeping is an activity of recording the financial transactions of the company in a	Accounting is an orderly recording and reporting of the financial affairs of an organization for

	systematic Manner.	a particular Period.
What is it?	It is the subset of accounting.	It is regarded as the language of Business.
Decision Making	On the basis of bookkeeping Records, decisions cannot be taken.	Decisions can be taken on the basis of accounting records.
Preparation of Financial Statements	Not done in the bookkeeping process	Part of Accounting Process
Tools Journal and Ledgers	Balance Sheet, Profit & Loss	Account and Cash Flow Statement
Methods / Sub-fields	Single Entry System of Bookkeeping and Double Entry System of Bookkeeping	Financial Accounting, Cost Accounting, Management Accounting, Human Resource Accounting, Social Responsibility Accounting.
Determination of Financial Position	Bookkeeping does not reflect the financial position of an organization.	Accounting clearly shows the financial position of the entity.

Advantages of Audit

Advantages of Audit to the business enterprise and Management:

(1) Accuracy or correctness of the books of accounts

(2) Authenticity and reliability of the financial statements.
(3) Detection and rectification of errors and frauds.

Advantages of audit to the owners of the business:

- In the case of a **sole trader**, auditing assures him that all business transactions have been duly accounted for and there are no errors or frauds.
- It also helps him to know the facts about the business.
- In the case of **partnership firm**, audited accounts serve as an
- **Evidence** of proper management of the affairs of the business.
- Audited accounts help in the valuation of goodwill and settlement of accounts on the admission, retirement or death of a partner.
- Again, audited accounts minimize the chances of disputes among the partners.
- In the case of a **joint stock company**, auditor of accounts assures the shareholders that the affairs of their company are smoothly and their investment is safe.
- The shareholders of a company can value their shares on the basis of audited accounts.
- In the case of a co – operative society or a trust, audit assures the members or the beneficiaries that the affairs of the society or trust are conducted properly.

Advantages of Auditing to others

- (1**) Lenders** can depend on audited financial statements while taking a decision to **grant credit** to the business concern.
- (2) **Tax authorities** can depend on audited statements in assessing sales tax, income tax and wealth tax of the business.
- (3) Audit of accounts safeguards the interests of the **workers and** is helpful in the settlement of claim for higher wages and bonus.
- **Insurance company** can rely on audited accounts to settle claims in respect of damage or loss of any business asset by fire, theft etc.
- (6) The **purchaser** of a business can easily calculate the amount of purchase consideration based on audited accounts.

LIMITATIONS OF AUDITING

- Extra Cost
- Dependence on opinions of others
- Conflict with others

- No assurance
- Detailed checking not possible
- Small concerns
- Faulty judgement
- Audit Program Increases the chance Of Fraud

QUALITIES OF AN AUDITOR:

1. Professionally Competent
2. Honest
3. Auditing Skills
4. Accounting Knowledge
5. Knowledge of Business Law
6. Knowledge of Taxation Law
7. Computer Expert
8. Knowledge Of management System
9. Preparation of Budget
10. Qualification
11. Intelligent
12. Tactful
13. Maintain Secrecy
14. Patience
15. Critical Attitude
16. Bold and Courageous
17. Courteous
18. Independent
19. Common Sense

OBJECTIVES OF AUDIT

PRIMARY OBJECTIVES OF AUDIT

1. Examining the system of internal check.
2. Checking arithmetical accuracy of books of accounts, verifying posting, casting, balancing etc.
3. Verifying the authenticity and validity of transactions.
4. Checking the proper distinction between capital and revenue nature of transactions.
5. Confirming the existence and value of assets and liabilities.
6. Verifying whether all the statutory requirements are fulfilled or not.
7. Proving true and fairness of operating results presented by income

8.Statement and financial position presented by the balance sheet.

SUBSIDIARY OBJECTIVES OF AUDIT

Detection and prevention of errors

1 .Errors of principle.
2 .Errors of omission.
3. Errors of commission.
4 .Compensating errors.

Detection and prevention of frauds

Misappropriation of cash.
Misappropriation of goods.
Manipulation of accounts or falsification of accounts without any misappropriation.

Under-or over-valuation of stock

Other objectives

To provide information to income tax authority.
To satisfy the provisions of Companies Act.
To have a moral effect.

SCOPE OF AUDIT

The scope of an audit is the determination of the range of the activities and the period of records that are to be subjected to an audit examination.

The scope of audit are;
Legal Requirements.
Entity Aspects.
Reliable Information.
Proper Communication.
Evaluation.
Test.
Comparison.
Judgments.

CLASSIFICATION OF AUDIT

On the basis of organizational structure.

- Statutory audit
- Private audit
- Government audit
- Internal audit

On the basis of conduct.

- Continuous audit
- Periodical audit
- Interim audit
- Partial audit
- Occasional audit
- Balance sheet audit
- Auditing in depth
- Standard audit

On the basis of functions and objective.

- Cost audit
- Management audit
- Social audit
- Performance audit
- Efficiency audit
- Cash audit
- Special audit
- Joint audit
- System audit
- Operational audit

STATUTORY AUDIT OR COMPULSORY AUDIT

Companies governed by the companies act, 1956.
Banking companies governed by the banking regulation act, 1949.
Electricity supply companies governed by the electricity supply act, 1948.
Co-operative societies registered under co-operative society's acts, 1912.
Societies registered under the society's registration act 1860.

FEATURES OF STATUTORY AUDIT

▶It is compulsory.
▶The auditor must be an independent person..
▶Qualified chartered accountant.
▶Appointed according to the norms laid down by the act.

PRIVATE AUDIT OR VOLUNTARY AUDIT

Not compulsory by law
In India : sole trading concerns, partnership firm and joint Hindu family.
Due to amendment in the income tax .

Professional auditor has been made compulsory in case of all business.

Government audit

Audit of government departments.

Statutory corporations or public corporations.

Government companies.

Internal audit

Continuous audit.

Appointed by the management.

Accounting system.

An employee of the business and acts as an adviser.

Submit the report to the management.

Verifies the books of accounts & other records.

Internal auditor removed by the management**.**

On the basis of conduct

Continuous audit:

-conducted throughout the year.

-detailed checking of books of accounts.

-more expensive.

-early detection of errors & frauds.

-frequent visit of auditor reduce the errors & frauds

Periodical Audit

-End of the year.

-Not permitted to checking.

-Less expensive.

-early detection is not possible.

-No such chance.

Interim audit

Conducted between two annual audits.

Complete checking of the accounts prepared by the Company.

Conducted between two periodical or two balance sheet audits.

Partial audit

Checking the part of the books of accounts.

-misappropriation of goods

- Purchase or sales books.

Undertaken only small firms,

Not permitted to large business.
Audit is compulsory.

Occasional audit

-desire of the owner of the business
-Not an regular basis.
-suspected any fraud and errors.

Balance sheet audit
Auditing In-depth

Based on functions and objectives

1. Cost Audit
2. Management Audit
3. Social Audit
4. Cash Audit
5. Special Audit
6. Operational Audit