

## COMMERCE

Dear Students of B.Com Hons. (Part 1, Paper II: Auditing)

Hope you all are fine and staying at home.

This is Prof. (Dr.) Reyazuddin, (Former Professor of Commerce, Patna University, presently working as the Chief Co-ordinator of Commerce and Management at Nalanda Open University, Patna) Guest Faculty, Magadh Mahila College, Patna University, Patna.

For the purpose of preparation of Annual Examination of 2020, I am sending you some valuable information. Kindly go through them.

What is Auditing?

Financial auditing is the process of examining an organization's (or individual's) financial records to determine if they are accurate and in accordance with any applicable rules (including accepted accounting standards), regulations, and laws.

External auditors come in from outside the organization to examine accounting and financial records and provide an independent opinion on these records. Law requires that all public companies have their financial statements externally audited.

Internal auditors work for the organization as internal employees to examine records and help improve internal processes such as operations, internal controls, risk management, and governance.

Audit is defined as the examination or inspection of various books of accounts by an auditor followed by physical checking of inventory to make sure that all departments are following documented system of recording transactions. It is done to ascertain the accuracy of financial statements provided by the organisation.

Description: Audit can be done internally by employees or heads of a particular department and externally by an outside firm or an independent auditor. The idea is to check and verify the

accounts by an independent authority to ensure that all books of accounts are done in a fair manner and there is no misrepresentation or fraud that is being conducted.

There are four main steps in the auditing process. The first one is to define the auditor's role and the terms of engagement which is usually in the form of a letter which is duly signed by the client.

The second step is to plan the audit which would include details of deadlines and the departments the auditor would cover. Is it a single department or whole organisation which the auditor would be covering. The audit could last a day or even a week depending upon the nature of the audit.

The next important step is compiling the information from the audit. When an auditor audits the accounts or inspects key financial statements of a company, the findings are usually put out in a report or compiled in a systematic manner.

The last and most important element of an audit is reporting the result. The results are documented in the auditor's report.

There are six essential features of auditing:

- Systematic process
- Three-party relationship
- Subject matter
- Evidence
- Established criteria
- Opinion

The objectives of an audit are divided into two parts: (i) primary objectives and (ii) subsidiary objectives.

## Primary Objectives of Audit

The main objectives of the audit are known as the primary objectives of the audit.

They are as follows:

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.

## Subsidiary Objectives of Audit

These are such objectives that are set up to help in attaining primary objectives.

They are as follows:

1. Detection and prevention of errors.
2. Detection and prevention of fraud.
3. Under-or over-valuation of stock.

An audit program is a set of policies and procedures that dictate how an evaluation of a business is done.

This generally involves specific instructions as to what, and how much, the evidence must be collected and evaluated, as well as who will collect and analyze the data and when this should be done.

These types of programs are used to check up-on things like a business' performance, finances, economy, and efficiency, and are generally tailored to a specific business or purpose.

It is a description, memorandum or an outline of the work to be done, prepared by an auditor for the guidance and control of the assistants. It provides a guide in arranging and distributing the work and in checking against the possibility of omissions.

### Objectives of the Audit Program

The objectives of the audit program are to:

1. Determine compliance with company policy and procedures.
2. Determine the effectiveness of the policy and procedures.
3. Determine the accuracy of reports generated by department personnel.
4. Evaluate the adequacy of internal controls.
5. Determine compliance with applicable state and federal regulations of the function under review.
6. Search for value-added recommendations that improve the efficiency and contribution of the function under review.

### Advantages of Audit Program

The advantages of audit program are:

- a. It provides a clear set of instructions on the work to be done.
- b. It provides a clear record of work done and by whom.
- c. Work can be reviewed by the senior auditors.
- d. Work will not be duplicated.
- e. No important work will be overlooked.
- f. Evidence of work done is available for use in defending charges for negligence.
- g. The audit program serves as a shield against any charge of negligence by a client on the part of the auditor.

- h. It assures that no material aspect of audit examination has been overlooked.
- i. It pinpoints the audit work to be done by audit staff and that has already been done.
- j. It facilitates the distribution of work among the audit staff according to their knowledge.
- k. The audit program of last year serves as a basis in preparing the audit program for the subsequent year.
- l. Before signing the audit report, the final review of the work done can be easily made.
- m. It ensures adherence to International Accounting and Auditing Standards.
- n. The responsibility of each audit staff (articled clerk) is fixed.

#### Disadvantages of Audit Program

The disadvantages of audit program are as follows:

- a. Work may become mechanical.
- b. Parts may be executed without regard to the whole scheme.
- c. A program may be rigidly followed.
- d. An initiative may be lost.
- e. Audit staff may not have the opportunity of showing independent thinking, intelligence, and initiative due to adherence to audit programs.
- f. Audit program may not cover everything that might come up during an audit,
- g. It may create rigidity in audit examination if not frequently reviewed and updated.
- h. Audit staff is' bound to follow audit program mechanically irrespective of changes in internal control introduced by the client.
- i. Audit staff may defend by claiming that a particular audit examination was not provided by an audit program.

- j. A fixed auditing program will have its limitations.
- k. Clients' staff knowing the extent and methods of checking followed by the auditor may devise means to escape detection of fraud by an auditor.
- l. Drawing up of an audit program may be unnecessary for a small concern.

The students are advised to read the above along with advantages and limitations of auditing; different methods of charging depreciation; audit of Banks and Insurance Companies. Advantages and disadvantages of Audit Note Book, kind of audit i.e., Annual audit, Continuous audit, interim audit, management audit, cost audit. Valuation and verification, secret reserve, capital and revenue expenditure.

Prof. (Dr.) Reyazuddin

Guest Faculty

Magadh Mahila College

Patna University