

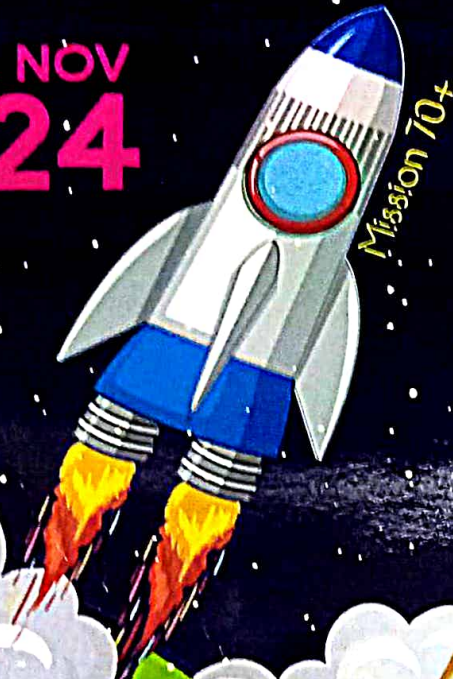
CA INTER



AUDITING & ETHICS

MULTI COLOR
CONCEPT BOOK

FOR MAY & NOV
2024



BY CA SANIDHYA SARAF

THE JOURNEY BEGINS



EVERY UPDATED

CA-INTER

AUDITING & ETHICS



CA SANIDHYA SARAF

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PREFACE

ABOUT THE AUTHOR

CA by Profession and Teacher by passion, CA Sanidhya Saraf is a young and dynamic faculty of Audit who has achieved a lot of fame and success in a short span of time.

His unique methodology of teaching Audit has made him very popular among students of CA and CMA fraternity.

He has taught more than 30000 students and mentored thousands of students to achieve success in Audit under his guidance.

This book of Inter Audit has been designed keeping in mind the examination requirement of students. It is presented in a simpler version in the form of charts and tables to facilitate ease of learning for students.

For any suggestions or value additions required to be incorporated in the material mail us at sanidhyasaraf@gmail.com

CHAPTER 01

BASIC DEFINITIONS IN AUDIT

1. Financial Reporting Framework (FRF)

A financial reporting framework refers to a set of rules, principles, and guidelines that companies use to prepare and present their financial statements to ensure consistency, comparability and transparency among users of financial statements.

There are mainly 2 types of framework

1. International Financial Reporting Standards - IFRS is a recognized International framework. MNCs use it worldwide for preparation and presentation of financial statement.
2. Local Generally Accepted Accounting principles- For example, US GAAP, UK GAAP , Indian GAAP etc.

Examples of Indian GAAP include Accounting Standards, Ind-AS, Schedule III, Companies Act etc.

2. True and Fair View-

True and fair view is a principle that governs financial reporting and auditing. It refers to the requirement that financial statements should provide a faithful representation of a company's financial position, performance, and cash flows, and that they should be free from material misstatements or errors.

The true and fair view principle is a fundamental concept in financial reporting, and it requires that financial statements be prepared with integrity, objectivity, and professional skepticism, and that they present a complete and accurate picture of a company's financial affairs.

To achieve a true and fair view, financial statements should be prepared in accordance with the applicable financial reporting framework, and applying sound Accounting principles and practices.

3. Professional skepticism -

Professional skepticism is a fundamental concept in auditing that requires auditors and accountants to approach their work with a questioning mind .It requires auditors to be alert to the possibility of fraud, errors, or misstatements in financial statements.

4. Misstatement-

Misstatement means a difference between

- The amount, classification, presentation or disclosure of a reported financial statement

And

- The amount, classification, presentation or disclosure that is required for the item to be in accordance with the applicable FRF.
- 5. **Assertion** - Assertion means representations made by management, explicit or otherwise, that are embodied in the financial statements. Audit Assertion simply means validating the claims made by the management in financial statements.
- 6. **Audit Risk** - Audit risk means risk of expressing inappropriate Audit opinion when the financial statements are materially misstated.
- 7. **Audit procedures** - Procedures performed by the auditor to obtain audit evidence and arrive at a opinion.

Classification of Audit Procedures

A. **Risk Assessment Procedures-**

Risk Assessment Procedures involves identifying and assessing the risk of material misstatement existing in financial statements.

It includes

- i. Inquires of management
- ii. Analytical Procedures
- iii. Observation and Inspection

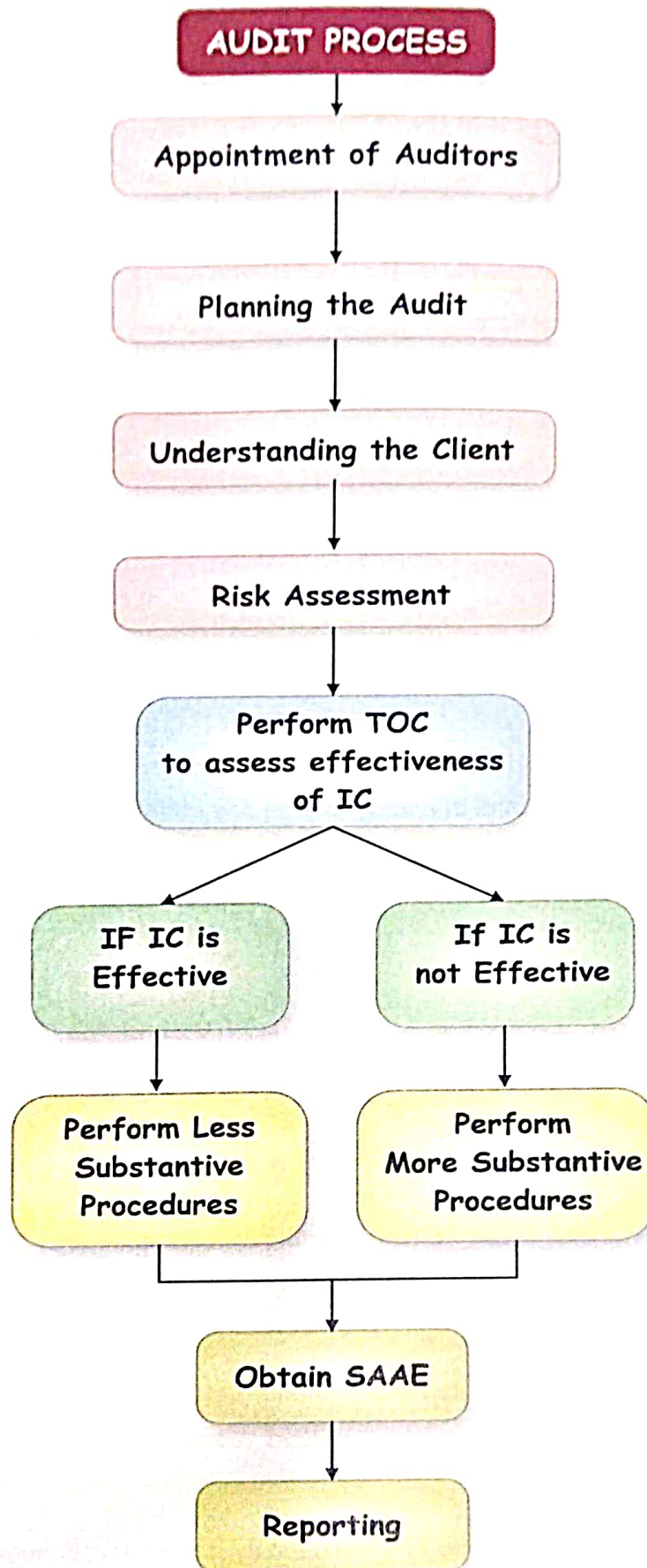
B. **Further Audit Procedures**

- 1. **Test of controls** - Procedures performed to assess the effectiveness of internal control system.
- 2. **Substantive Procedures** - Substantive Procedures are used to detect material misstatements in the financial statements.

It includes

- Test of Details of Account Balances, class of transactions and disclosure.
- Substantive Analytical Procedures

- 8. **Substantive Analytical Procedures** - It involves ratio analysis and examining relationships between financial and non-financial data to identify potential misstatements in financial statements. They are also known as Analytical review Procedures.

9. Audit Process

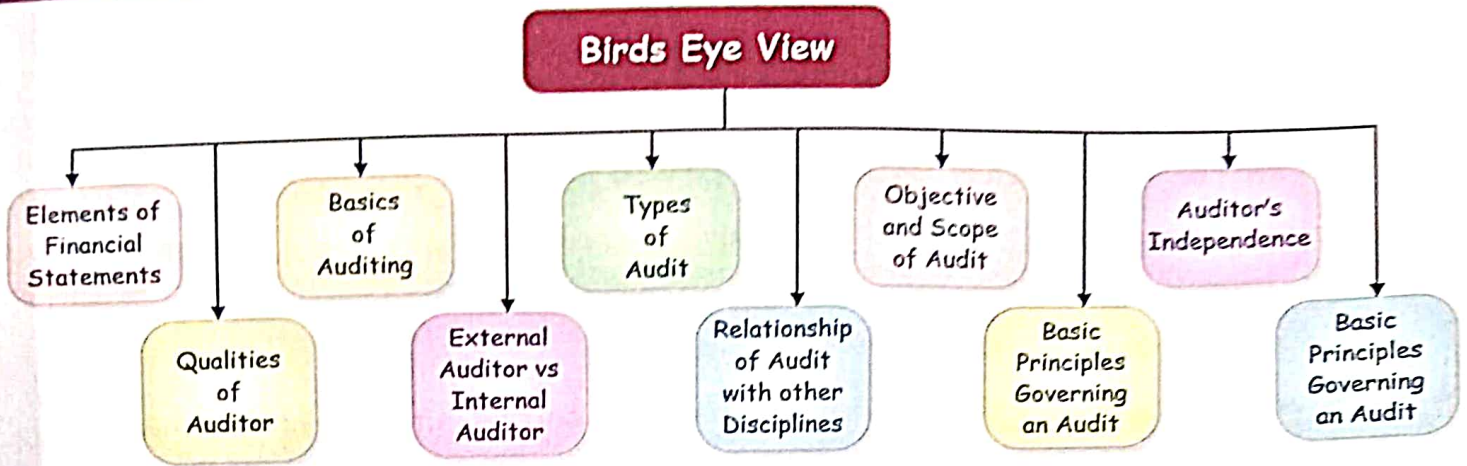
10. Link between IC, ROMM & AP

Strength of IC	ROMM	Extent of A.P.
IC is effective	Low ROMM	Less A.P
IC is not effective	High ROMM	More A.P

Space for Notes

CHAPTER 02

NATURE, OBJECTIVE & SCOPE OF AUDIT

**1. ELEMENTS OF FINANCIAL STATEMENTS****Elements of F.S.**

- ❖ Conceptual Framework for the Preparation and Presentation of F.S." Issued by ASB of ICAI sets out the concept that underlie the preparation and presentation of F.S. for external users.
- ❖ A complete set of financial statements normally includes
 - A Balance Sheet
 - A Statement of Profit & Loss
 - Cash Flow Statement, and
 - Those notes and other statements and explanatory material that are an integral part of the financial statements.

Periodicity & Users

Such financial statements are prepared and presented at least annually and are directed toward the common information needs of a wide range of users

Inclusions

Financial statements may also include supplementary schedules and information based on such statements for example, information about business and geographical segments.

Exclusions

Directors Report, Chairman Statements, discussion and analysis by management and similar items that may be included in a financial or annual report.

2. ACCOUNTING, AUDITING & INVESTIGATION

Auditing

- * Audit is an independent examination
- * of Financial Information
- * of any entity whether profit making or not, irrespective of its size and legal structure
- * when such an examination is conducted with a view to express an opinion thereon

The person conducting this task should take care to ensure that financial statements would mislead anybody.

This he can do honestly by satisfying himself that:

- ❖ The accounts have been drawn up with reference to entries in the books of account.
- ❖ The entries in the books of account are adequately supported by sufficient and appropriate evidence.
- ❖ None of the entries in the books of account has been omitted in the process of compilation and nothing which is not in the books of account has found place in the statements.
- ❖ The information conveyed by the statements is clear and unambiguous.
- ❖ the financial statement amounts are properly classified, described and disclosed in conformity with accounting standards; and
- ❖ The statement of accounts present a true and fair picture of the operational results and the assets and liabilities.

2.1 Accounting vs Auditing

Basis	Accounting	Auditing
Meaning	It is an art of recording, classifying and summarizing financial transactions.	It involves independent examination of financial information.
Objective	To Prepare Financial Statement.	To express an opinion on true and view of financial statements.
Responsibility	Management is primarily responsible for maintenance of accounts.	Audit is carried out by an independent auditor.
Timing	Accounts are being prepared first prior to get them audited.	Auditing begins when accounts ends.

2.2 Auditing vs Investigation

Basis	Audit	Investigation
Objective	To verify whether the financial statements display a true and fair view of the state of affairs and the working results of an entity.	It aims at establishing a fact or a happening or at assessing a particular situation.
Scope	The scope of audit is wide and is determined by the provisions of relevant law in case of statutory audit.	The scope of investigation may be governed by statute or it may be non-statutory.
Periodicity	The audit is carried on either quarterly, half yearly or yearly.	The work is not limited by rigid time frame.
Nature	Involves tests checking to collect evidences for forming a judgement.	Requires a detailed study and examination of facts and figures.
Inherent Limitation	Audit suffers from inherent limitation.	No inherent limitation owing to its nature of engagement.
Evidence	Audit is mainly concerned with prima-facie evidence.	It seeks conclusive evidence.
Observance of Accounting Principles	Is governed by compliance with generally accepted accounting principles, audit procedures and disclosure requirements.	It is analytical in nature and requires thorough mind, capable of observing, collecting and evaluating facts.
Reporting	The outcome is reported to the owners of the business.	The outcome is reported to the person(s) on whose behalf investigation is done.

3. TYPES OF AUDIT-STATUTORY AUDIT & VOLUNTARY AUDIT**Audit Required Under Law**

- Companies governed by the Companies Act, 2013.
- Banking companies governed by the Banking Regulation Act, 1949.
- Electricity supply companies governed by the Electricity Supply Act, 1948.
- Co-operative societies registered under the Co-operative Societies Act, 1912.
- Public and charitable trusts registered under various Religious and Endowment Acts.
- Corporations set up under an Act of Parliament or State Legislature such as the LIC of India.
- Specified entities under various sections of the Income-tax Act, 1961.

Voluntary Audits

- ❖ Audits of the accounts of proprietary entities, partnership firms, HUF, etc.
- ❖ In respect of such entities, there is no basic legal requirement of audit.
- ❖ Many of such enterprises as a matter of internal rules require audit.
- ❖ Some may be required to get their accounts audited on the directives of Government for various purposes like sanction of grants, loans, etc.
- ❖ But the important motive for getting accounts audited lies in the advantages that follow from an independent professional audit.

4. OBJECTIVES & SCOPE OF AUDIT - SA 200**Objectives of Audit**

As per SA-200 "Overall Objectives of the Independent Auditor", in conducting an audit of financial statements, the overall objectives of the auditor are:-

- a) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement; and
- b) To report on the financial statements, and communicate as required by the SAs, in accordance with the auditor's findings.

Scope of Audit

The following points merit consideration in regard to scope of audit:-

- a) Terms of the Audit Engagement
- b) Requirement of Relevant Statute
- c) Pronouncement of the ICAI

However, the terms of engagement cannot supersede the requirements of statutory pronouncements of ICAI.

The following areas are generally covered in scope of Audit:-

1. The audit should be organized to cover adequately all aspects of the enterprise relevant to the financial statements being audited.
2. To form an opinion on the financial statements, the auditor should be reasonably satisfied as to whether the information contained in the underlying accounting records and other supporting data is reliable and sufficient as the basis for the preparation of the financial statements.

3. In forming his opinion, the auditor should also decide whether the relevant information is properly disclosed in the financial statements subject to statutory requirements, where applicable.
4. Making a study and evaluation of accounting systems and internal controls.
5. The auditor determines whether the relevant information is properly disclosed in the financial statements by
 - a) Comparing the financial statements with the underlying accounting records and other source data to see whether they properly summarize the transactions and events recorded therein
 - b) Considering the judgements the management has made in preparing the financial statements accordingly, the auditor assess the selection and consistent application of accounting policies, the manner in which the information has been classified and the adequacy of disclosure.
6. The auditor is not expected to perform duties which fall outside the scope of his competence. For example, the professional skill required of an auditor does not include that of a technical expert for determining physical condition of certain assets.
7. Constraints on the scope of the audit of financial statements that impair the auditor's ability to express an unqualified opinion on such financial statements should be set out in his report, and a qualified opinion or disclaimer of opinion should be expressed as appropriate. {SA 705}.

4.3 Areas outside the scope of Audit

- ❖ Auditor is not expected to perform duties which fall outside domain of his competence. For example, physical condition of certain assets like that of sophisticated machinery cannot be determined by him. Similarly, it is not expected from an auditor to determine suitability and life of civil structures like buildings.
- ❖ An auditor is not an expert in authentication of documents. The genuineness of documents cannot be authenticated by him because he is not an expert in this field.
- ❖ An audit is not an official investigation into alleged wrong doing. He does not have any specific legal powers of search or recording statements of witness on oath which may be necessary for carrying out an official investigation.

An overview of scope of Audit

Check box	Scope of audit of financial statements
✓	Coverage of all aspects of entity relevant to the financial statements being audited
✓	Reliability and Sufficiency of financial information
✓	Proper disclosure of financial information
✓	Expression of an opinion on financial statements
☒	Responsibility of preparation and presentation of financial statements
☒	Duties outside scope of competence of auditor
☒	Expertise in authentication of documents
☒	Investigation

5. AUDITOR'S INDEPENDENCE**5.1 Advantages of Independent Audit**1. **Protect the interest of fund providers**

It safeguards the financial interests of persons who are not associated with the management of the organisation e.g. partners or shareholders.

2. **Moral Check on Employees**

It acts as a moral check on employees from committing defalcations or embezzlement.

3. **Settlement of Taxes, etc.**

Auditing statement of accounts are helpful in settling of taxes, negotiating loans and determining the purchase consideration for a business.

4. **Detection of Wastages**

Audited statements also helps in detection of wastages and losses and shows the different ways by which these might be checked especially those that occurred due to absence, inadequacy of internal checks or Internal control measures.

5. **Proper Management of Books of Account**

Independent audit ascertain whether the necessary books of accounts and allied records have been properly kept and the client in making good deficiencies or inadequacies in this respect.

6. **Appraisal of Controls**

As an appraisal function, audit reviews the existence and operations of various controls in the organisation and reports weakness, inadequacies etc.