

Auditing-Basic Concepts

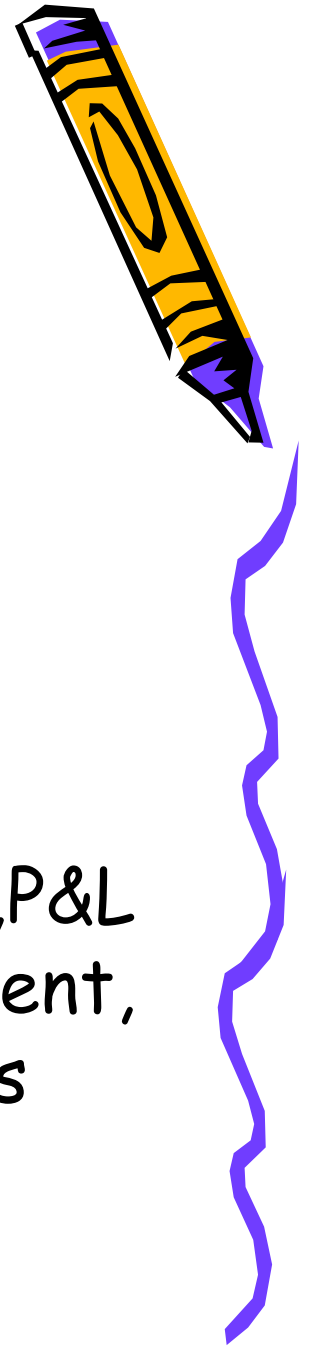
By
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Financial Reporting Framework

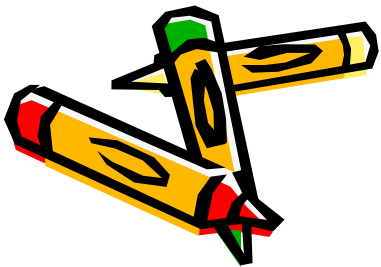
- Statutory & legal requirements
- Accounting standards
- Guidance Notes by ICAI
- Audit & Financial reporting framework
- Financial Statements-Balance sheet, P&L statement, Cash Flow statement, statements/notes appended to accounts

Exclusions from FS

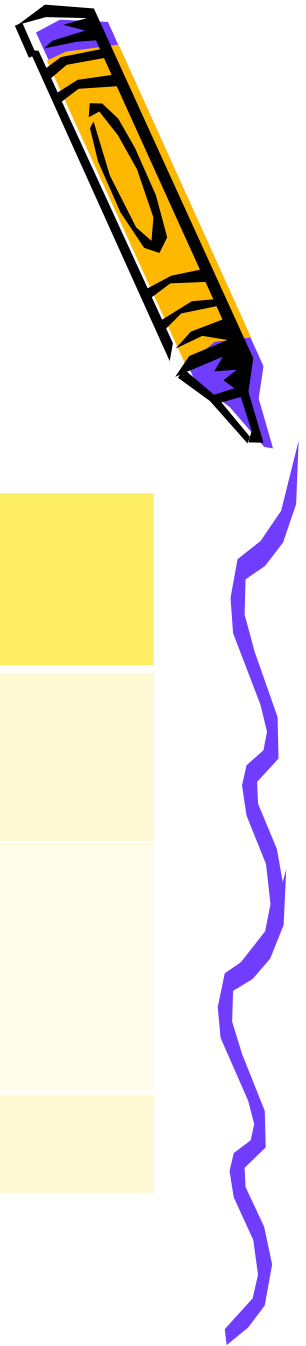


- Responsibility to prepare FS
- Users of financial statements
- Audit-as defined by ICAI

Auditing is the independent examination of financial information of any 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.



Objectives of audit



Financial audits

Other audits

Basic object- True & Fair view

Internal audit

Incidental object-
Detecting errors &
frauds

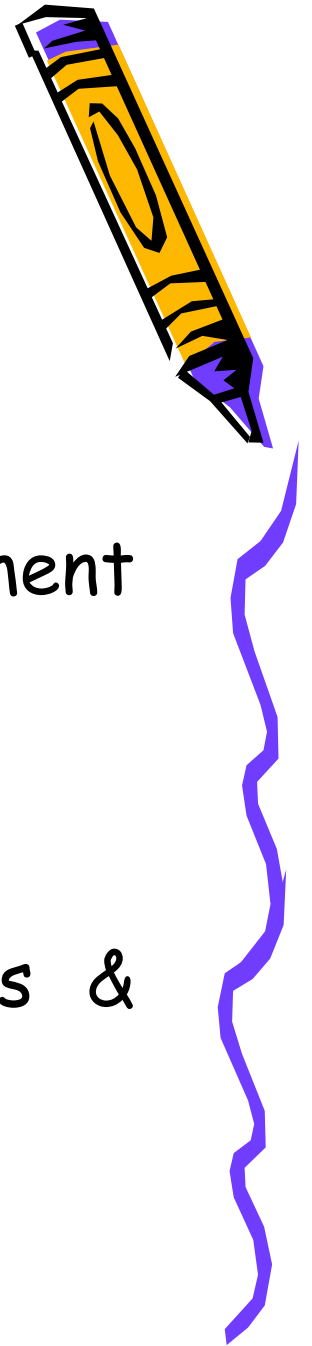
Cost audit

Tax audit



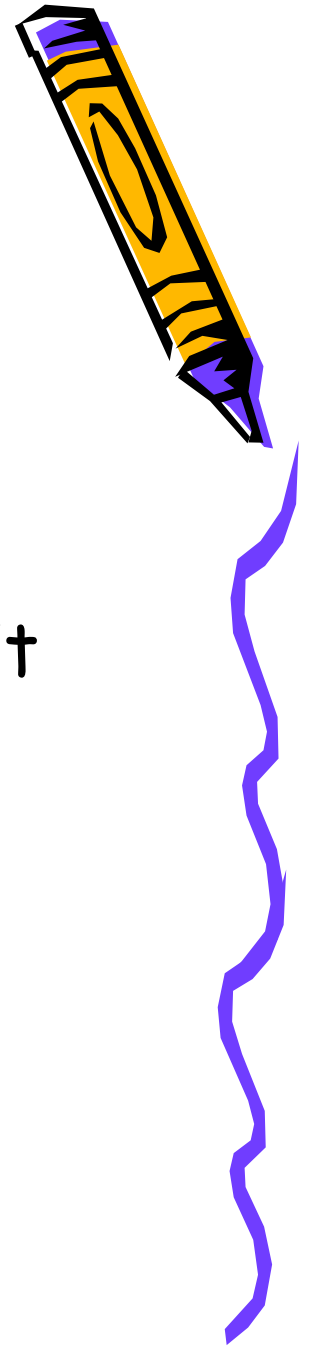
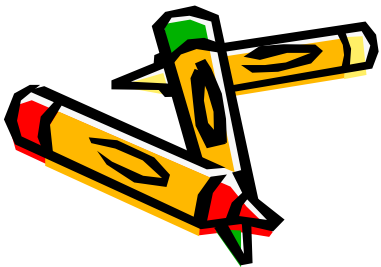
True & Fair view

- True & fair view of financial position & profit or loss
- Neither overstatement or understatement of financial position & profit/loss
- All material items are disclosed
- Compliance with law
- Compliance with accounting standards & principles

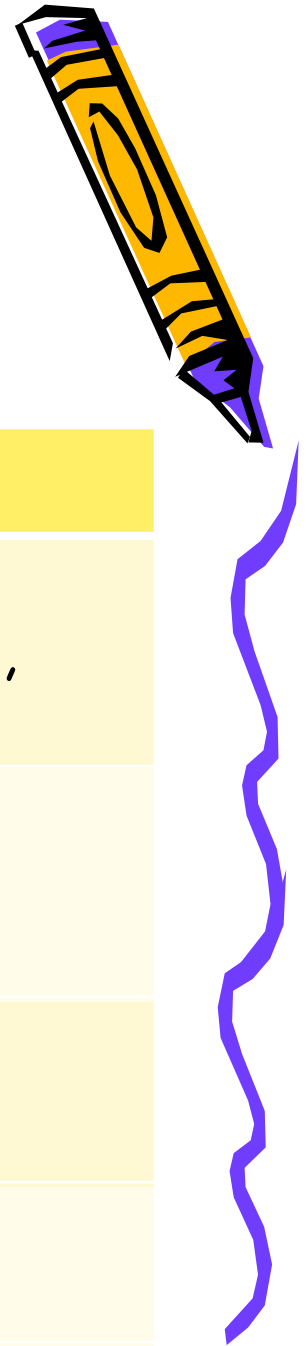


Detection of errors & frauds

- Primary responsibility of management
- Internal control procedures
- Review by auditor during course of audit
- Reporting to management
- No reporting on future prospects/efficiency/effectiveness of management



Errors-unintentional mistakes

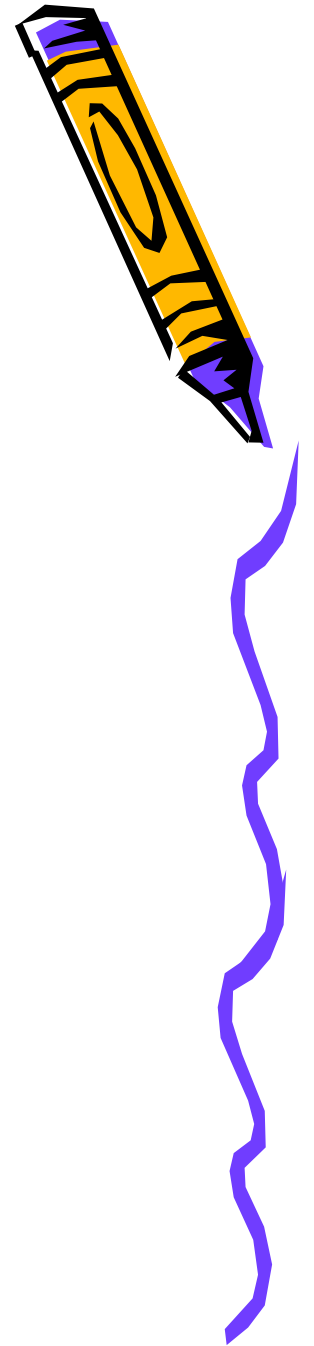


Errors of Principle	Clerical errors
Overvaluation or undervaluation of stock	Errors of omission - omission of transaction, partly or fully
Depreciation	Errors of commission- Errors in calculations, castings, postings
Capital & revenue expenditure	Compensating errors Errors of duplication
Accrual of income & expenses	



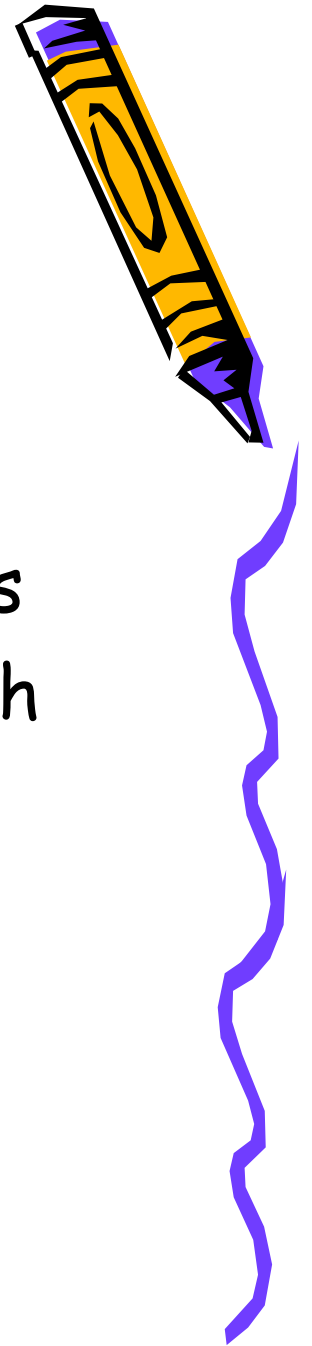
Detection of Errors

- Ledger scrutiny
- Checking the trial balance
- Nature of account & balance
- Difference divided by 2
- Difference divisible by 9



Frauds

- Not recording transactions
- Dummy transactions
- Wrong application of accounting policies
- Mis-appropriation of cash received/cash payments/cash balance
- Mis-appropriation of goods
- Teeming & lading



Window dressing

- Objective

Mis-leading investors/lenders/hide losses/higher commission

- Methods

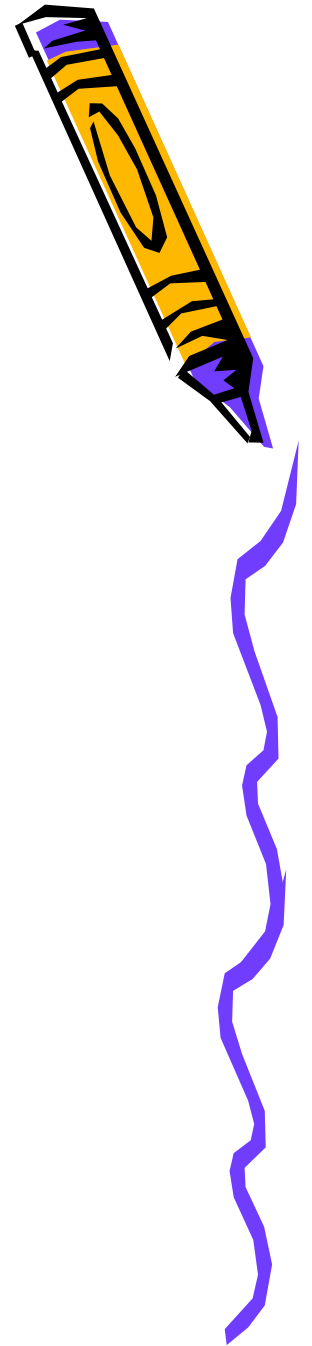
Overstatement of assets

Understatement of liabilities

Overstatement of profits

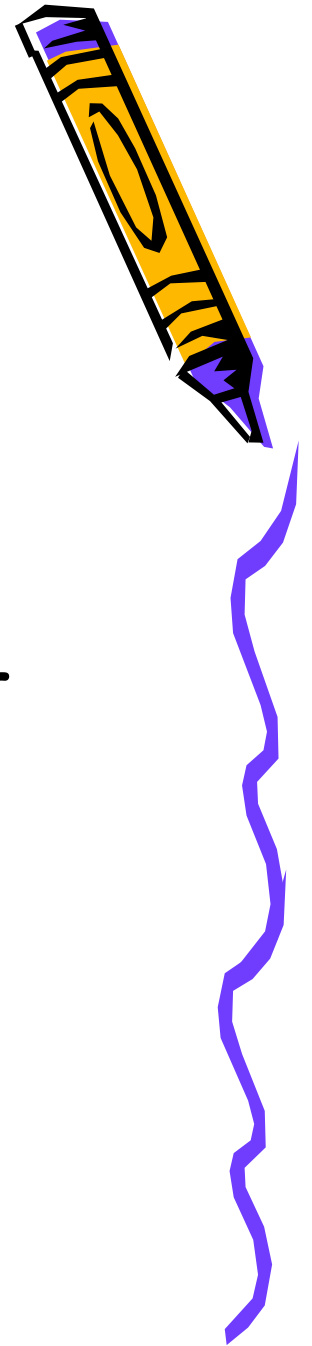
Understatement of expenses

- Penalties under Companies Act



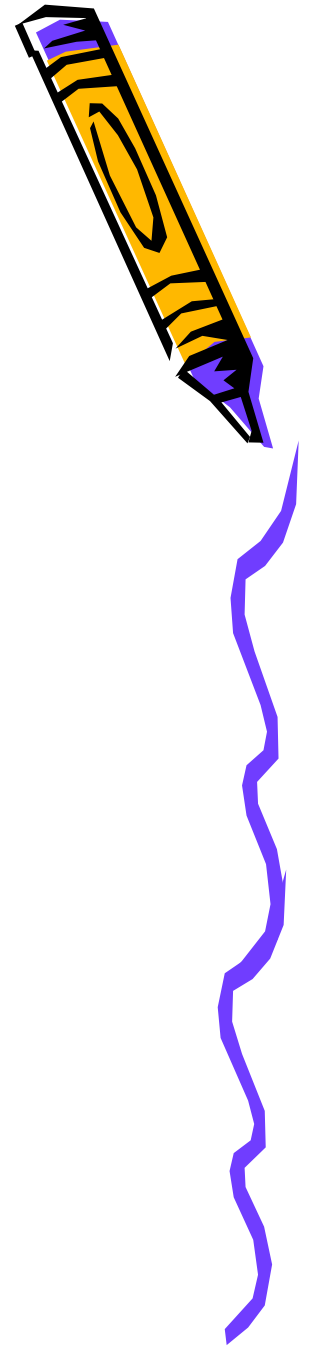
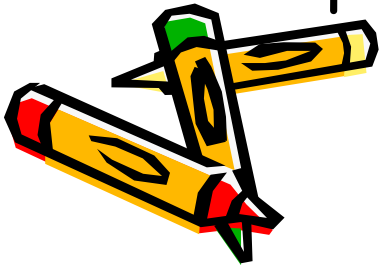
The effects of window dressing

- No true & fair view
- Shareholders are affected
- Hiding inefficiency of management
- Frauds by management
- Penalties & prosecution



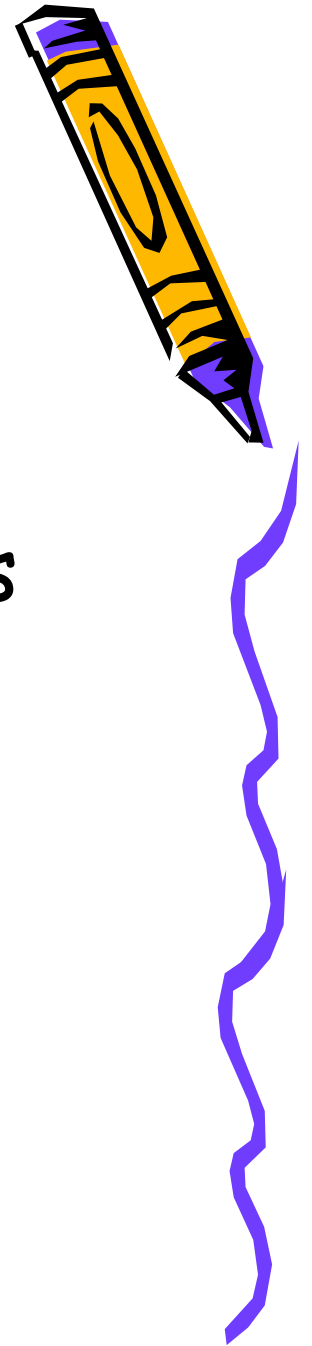
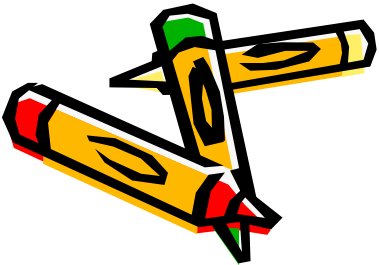
Auditor's duty regarding Window dressing/secret reserves

- Verification of income
- Verification of assets & liabilities
- Verification of provisions
- Verification of cash & closing stock
- Changes in method of accounting
- Deviation from GAAP & AS
- Report regarding true & fair view
- Report to Central Govt



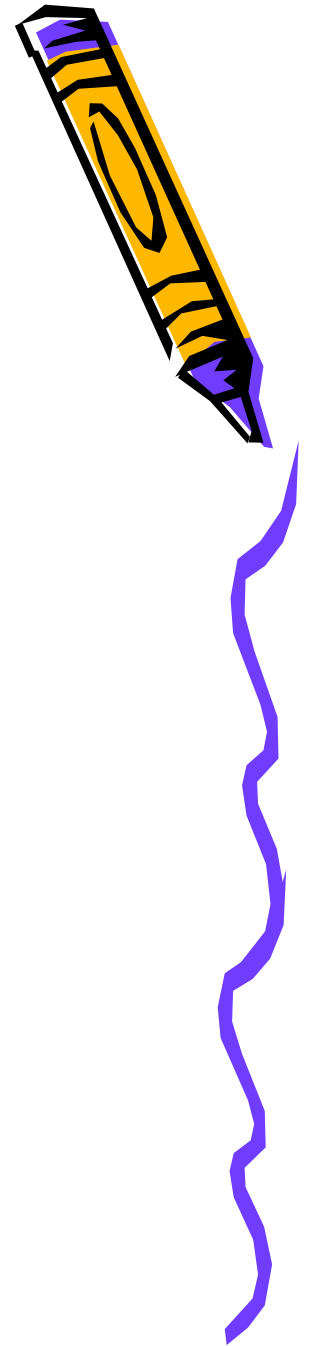
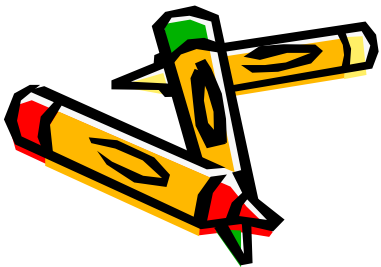
Secret Reserves

- Meaning - an amount by which NW has been deliberately understated
- Objectives behind secret reserves
 - Mis-lead competitors
 - Hide abnormal profits
 - Frauds
 - Banks are legally allowed



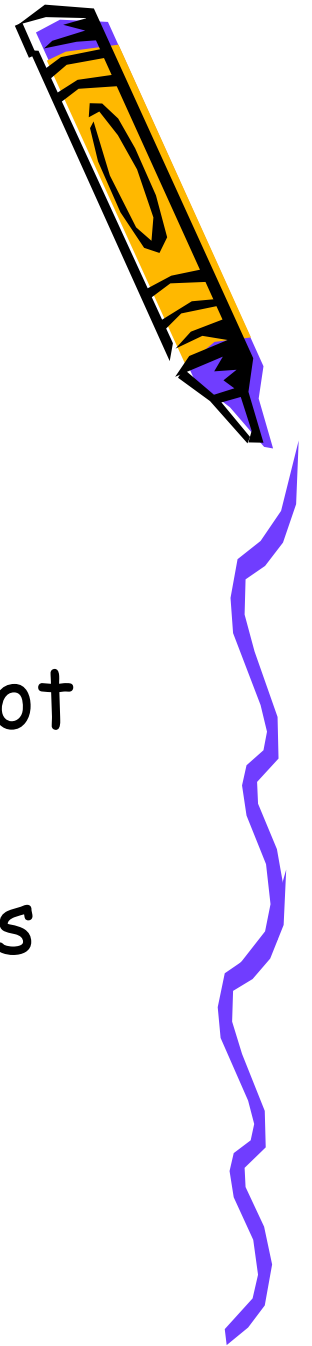
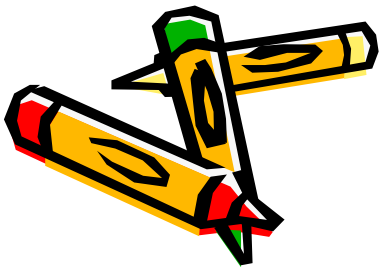
Creation of secret reserves

- Understatement of assets
 - Assets shown at lower cost
 - Excess depreciation
 - Undervaluation of stock
 - Excess provision for expenses
 - Write offs
 - Capital & revenue expenses
 - Accrued income, prepaid expenses



Creation of secret reserves Overstatement of liabilities

- Excessive provisions
- Providing contingent liabilities
- Ignoring write backs of amounts not payable
- Bogus bills for purchases/expenses
- Income received in advance



Principles of audit

Integrity, objectivity & independence

Companies Act, 2013- appointment , removal, qualification, dis qualification, remuneration, rights, non audit services

Chartered Accountants Act

Full disclosure

Audit Planning

Audit evidence

Evaluation of internal controls

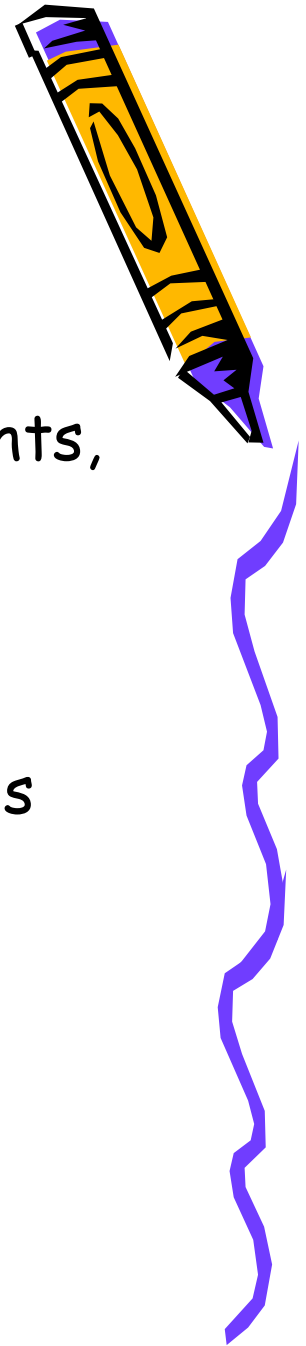
Reporting

Materiality

Confidentiality

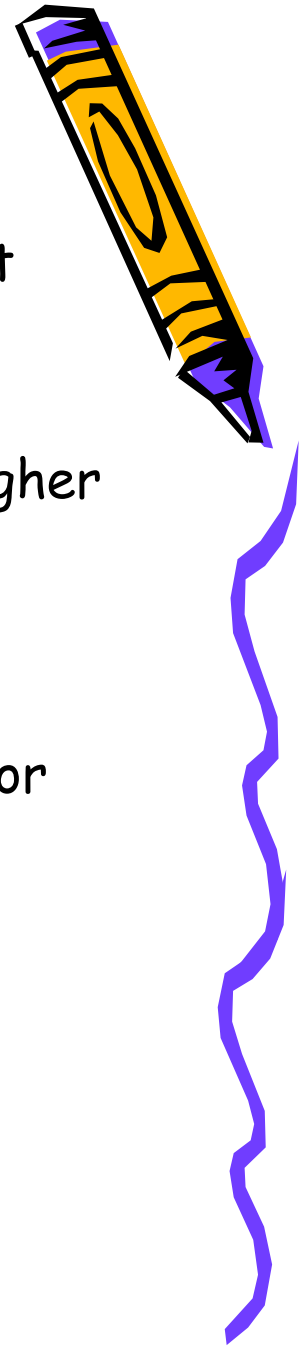
Skill & competence

Work done by others



Materiality

- Information is material if its omission or mis statement influences decision of users
- Impact of items either individually or in aggregate
- Expense being 1% of revenue of Rs.100,000 which is higher
- Comparative numbers for previous year
- Specific disclosures like fx transactions, consumption, managerial remuneration etc
- Extra ordinary items, ordinary items in some cases, prior period items & changes in accounting policies



Thank You

