

CONTEMPORARY

AUDIT

UNIT-III

Government Audit

Government audit is an independent and objective evaluation of the financial and non-financial activities of government entities. The primary objective of government auditing is to ensure that government entities are using public resources efficiently, effectively, and ethically.

Government auditing is typically conducted by a government audit agency, which is separate from the government entity being audited. The audit agency is responsible for examining the financial and non-financial records of the government entity, and providing an opinion on the fairness and accuracy of the information presented.

There are several types of government audits, including financial audits, performance audits, and compliance audits.

- **Financial audits:** These audits focus on the financial statements of the government entity, including its revenue, expenditures, and assets. The purpose of financial audits is to provide assurance that the financial statements are presented fairly and accurately, and that they comply with applicable accounting standards and regulations.
- **Performance audits:** These audits focus on the efficiency, effectiveness, and economy of government programs and activities. The purpose of performance audits is to identify opportunities for improvement and to ensure that public resources are being used in the most effective and efficient manner possible.
- **Compliance audits:** These audits focus on whether government entities are complying with laws, regulations, and policies related to the use of public resources. The purpose of compliance audits is to identify instances of non-compliance and to recommend corrective action as necessary.

In addition to these types of audits, government audit agencies may also conduct special audits or investigations in response to specific issues or concerns.

Government Audit Components

The components of a government audit depend on the type of audit being conducted, but some common components include:

- **Planning:** The audit begins with planning, which includes defining the scope and objectives of the audit, identifying the areas to be audited, and developing an audit plan.
- **Risk Assessment:** The audit team performs a risk assessment to identify and prioritize the areas of highest risk for the auditee entity. This step helps the audit team to focus its efforts on areas where there is a higher likelihood of errors, fraud, or non-compliance.
- **Fieldwork:** The audit team conducts fieldwork, which includes collecting and analyzing data, reviewing documents, and interviewing key personnel. This step is critical for understanding the operations of the auditee entity and assessing its compliance with applicable laws and regulations.

- **Testing:** During the fieldwork phase, the audit team performs testing to evaluate the effectiveness of internal controls and to assess the accuracy of financial and other information. This may include testing of transactions, balances, and other data.
- **Reporting:** Once the audit team completes the fieldwork and testing, they prepare a report that summarizes their findings and recommendations. The report may include recommendations for improving internal controls, ensuring compliance with laws and regulations, and enhancing the effectiveness and efficiency of operations.
- **Follow-up:** After the audit report is issued, the audit team may conduct follow-up activities to ensure that the recommendations are implemented and that the auditee entity has taken appropriate corrective action.
- **Quality Assurance:** Government audit agencies typically have a quality assurance process in place to ensure that audits are conducted in accordance with applicable standards and that audit reports are accurate and reliable.

Government Audit agency in INDIA

In India, the main agency responsible for government audits is the Comptroller and Auditor General (CAG) of India. The CAG is an independent constitutional authority that is responsible for auditing the accounts of the central and state governments, as well as public sector undertakings and other bodies that receive government funding.

The CAG is appointed by the President of India and is responsible for conducting audits that provide an independent and objective evaluation of government operations, finances, and compliance with laws and regulations. The CAG is also responsible for submitting audit reports to Parliament, which are then discussed and debated by Members of Parliament.

In addition to the CAG, there are other government audit agencies in India that are responsible for conducting audits at the state and local levels. These include state audit departments, local audit offices, and other agencies that are responsible for ensuring transparency and accountability in government operations.

Audit of Limited Companies

Audit of Limited Companies is a process of reviewing the financial statements of a company to provide an independent and objective assessment of its financial position and performance. The audit is conducted by a qualified and independent auditor who examines the financial records of the company and provides an opinion on the accuracy and completeness of the financial statements.

The Companies Act, 2013 in India mandates that every company registered under it should get its accounts audited every year.

The following are the major steps involved in the audit of limited companies:

- **Planning:** The auditor plans the audit process, including the scope of the audit, the audit strategy, and the audit timetable.
- **Risk Assessment:** The auditor assesses the risks associated with the company's financial statements, including the risk of material misstatement, fraud, and non-compliance with laws and regulations.
- **Internal Control Evaluation:** The auditor evaluates the company's internal controls and determines the extent to which reliance can be placed on them.
- **Audit Evidence:** The auditor collects audit evidence by reviewing the company's financial records, including its accounting policies, books of accounts, and other financial documents.
- **Audit Procedures:** The auditor performs audit procedures, including analytical review, tests of detail, and other audit procedures to verify the accuracy and completeness of the financial statements.
- **Reporting:** The auditor prepares an audit report that includes an opinion on the accuracy and completeness of the financial statements, along with any findings, observations, or recommendations.
- **Follow-Up:** The auditor may follow up with the company to ensure that any recommendations have been implemented.

Audit of Limited Companies objectives

- **To provide an independent and objective assessment of the financial statements:** The audit provides an independent and objective opinion on the accuracy and completeness of the financial statements, which helps to assure stakeholders that the company's financial statements are reliable.
- **To ensure compliance with laws and regulations:** The audit helps to ensure that the company is complying with all relevant laws and regulations, including accounting standards, tax laws, and company law.
- **To detect and prevent fraud:** The audit helps to detect and prevent fraud and other financial irregularities by identifying any material misstatements or omissions in the financial statements.

- **To identify areas for improvement:** The audit helps to identify areas where the company's financial management and reporting practices could be improved, including internal controls, financial management systems, and accounting policies.
- **To provide assurance to stakeholders:** The audit provides assurance to stakeholders, including shareholders, creditors, and other interested parties, that the company's financial statements are reliable and accurate.
- **To enhance the credibility of the company:** The audit helps to enhance the credibility of the company by demonstrating its commitment to transparency, accountability, and good governance.

Advantages:

- **Increased Credibility:** An independent auditor's report provides assurance to stakeholders that the financial statements of the company are reliable and accurate, which can enhance the credibility of the company.
- **Compliance:** An audit helps to ensure compliance with laws and regulations, including tax laws, accounting standards, and company law.
- **Fraud Detection:** An audit can help detect and prevent fraud and other financial irregularities by identifying any material misstatements or omissions in the financial statements.
- **Improved Financial Reporting:** An audit can help to identify areas where the company's financial management and reporting practices could be improved, including internal controls, financial management systems, and accounting policies.
- **Better Decision-Making:** An audit report can provide valuable information to stakeholders for making informed decisions, such as investing in the company, lending money, or acquiring the company.

Disadvantages:

- **Cost:** The cost of an audit can be significant, particularly for smaller companies, which can impact profitability.
- **Time-Consuming:** The audit process can be time-consuming, particularly for larger companies with complex financial transactions, which can impact day-to-day operations.
- **Limited Scope:** The audit is focused on financial statements and may not cover other areas of the business, such as operational efficiency or strategic planning.
- **Limited Liability:** The auditor's liability is limited, which may reduce the level of assurance provided to stakeholders.
- **Limited Independence:** The auditor's independence may be compromised if they have a long-standing relationship with the company or if they provide non-audit services to the company.

Company Auditor in INDIA, Appointment, Remuneration, Powers, Duties and Liabilities

In India, the Companies Act, 2013 regulates the appointment, rights, duties, and removal of auditors of companies. The Act requires all companies registered under it to appoint a qualified auditor to audit their financial statements.

Company auditors in India play a crucial role in ensuring the accuracy and reliability of financial statements of companies registered under the Companies Act, 2013. They are appointed by the company's board of directors, subject to approval by the shareholders, and have certain rights and duties, including the preparation of an audit report.

The following are some key points related to company auditors in India:

- **Appointment:** The auditor of a company is appointed by the company's board of directors, subject to approval by the company's shareholders. The appointment is for a period of one year and can be renewed for a maximum of five years.
- **Eligibility:** To be eligible for appointment as an auditor of a company in India, the person or firm must be a practicing chartered accountant and registered with the Institute of Chartered Accountants of India (ICAI).
- **Rights and Duties:** The auditor has the right to access all the company's books, records, and vouchers, and to obtain information and explanations from the company's officers. The auditor's duties include examining and reporting on the company's financial statements, evaluating internal control systems, and reporting any fraud or non-compliance with laws and regulations.
- **Removal:** The auditor can be removed by the company's shareholders before the end of their term only through a special resolution and with prior approval from the Central Government.
- **Audit Report:** The auditor's report includes an opinion on the true and fair view of the company's financial statements, along with observations on any significant matters arising from the audit.
- **Penalties:** The Companies Act, 2013 provides for penalties in case of non-compliance with audit requirements, including fines and imprisonment for company officers.

Examples of sources of an auditor's power are:

- **Legal Provisions:** The Companies Act, 2013 in India and other relevant laws provide auditors with the legal power to access company books and records, obtain information from company officers, and report on any non-compliance or fraud.
- **Auditing Standards:** Auditing standards issued by various professional bodies, such as the Institute of Chartered Accountants of India (ICAI) and the Institute of Internal Auditors (IIA), provide auditors with guidelines on how to carry out their work effectively and efficiently.

- **Terms of Engagement:** The terms of engagement or the audit engagement letter between the auditor and the company define the scope of the audit, the responsibilities of the auditor and the company, and the fees and expenses involved. These terms provide the auditor with the power to perform the audit within the agreed-upon scope and access the required information and resources.

Remuneration

The remuneration of a company auditor is determined by the Board of Directors or the Audit Committee of the company, based on the recommendations of the Statutory Auditors. The remuneration is subject to the approval of the shareholders of the company at the Annual General Meeting.

In India, the Companies Act, 2013 provides for the remuneration of the company auditor. Section 142 of the Act specifies that the remuneration of the auditor shall be determined by the company in a general meeting or by the Board of Directors or the Audit Committee, as may be decided by the company in the general meeting.

The Act further provides that the remuneration of the auditor may include reimbursement of expenses incurred by the auditor in connection with the audit, and also any fees paid to the auditor for any other services rendered by them to the company.

It is important to note that the remuneration of the auditor should be reasonable and commensurate with the services rendered by them. Excessive remuneration may create a conflict of interest and compromise the independence of the auditor, which is essential for carrying out an effective audit.

Duties:

- Expressing an opinion on the financial statements of the company based on the audit conducted.
- Ensuring compliance with the provisions of the Companies Act, 2013 and other applicable laws.
- Verifying and validating the books of accounts, records and other relevant documents of the company.
- Reporting to the members of the company on any fraud or suspected fraud committed in the company.
- Reporting to the members of the company on any material misstatement or omission in the financial statements of the company.
- Reporting to the members of the company on any deficiencies in the internal controls of the company.

Liabilities:

- The auditor is liable for any loss suffered by the company due to their negligence or misconduct in carrying out the audit.

- The auditor is also liable for any misstatement or omission in the audit report, which results in a loss to the company or its stakeholders.
- The auditor is required to disclose any conflict of interest that may affect their independence and objectivity in carrying out the audit.
- The auditor is required to maintain confidentiality of the information obtained during the course of the audit, and not disclose such information without the permission of the company or its management.
- The auditor is required to comply with the Code of Ethics issued by the Institute of Chartered Accountants of India (ICAI) and other relevant regulatory bodies.

Audit Report, Components, Types, Sample

An audit report is a formal document prepared by the auditor after the completion of an audit, which provides an opinion on the financial statements of the company. The report summarizes the auditor's findings, observations and conclusions after reviewing the financial records of the company, and highlights any issues or concerns that the auditor may have come across during the course of the audit.

The audit report is an important tool for stakeholders to assess the financial health and performance of the company, and it serves as a means of providing assurance that the financial statements are reliable and accurate.

The format of an audit report typically includes the following components:

- **Title:** This includes the name of the audit firm and the name of the company being audited.
- **Addressee:** This includes the name of the stakeholders who will receive the report, such as the shareholders, Board of Directors or the management of the company.
- **Introductory paragraph:** This describes the scope and objectives of the audit, as well as the period covered by the audit.
- **Management's responsibility:** This describes the responsibility of the management of the company in preparing and presenting the financial statements, and maintaining effective internal controls over financial reporting.
- **Auditor's responsibility:** This describes the responsibilities of the auditor in conducting the audit and expressing an opinion on the financial statements of the company.
- **Opinion:** This includes the auditor's opinion on the fairness of the financial statements and whether they are presented in accordance with the applicable accounting standards.
- **Basis of opinion:** This describes the methodology used by the auditor in conducting the audit and forming their opinion, as well as any limitations or restrictions on the audit.
- **Key audit matters:** This section highlights any significant issues or concerns that the auditor may have come across during the course of the audit.
- **Other information:** This includes any other information that the auditor may wish to highlight, such as the auditor's independence or any other matters of significance.
- **Signature and date:** This includes the signature of the auditor and the date on which the report was prepared.

Audit Report Types

There are various types of audit reports that can be issued by auditors depending on their findings during the audit. Some of the common types of audit reports are:

- **Unqualified opinion:** This is the most common type of audit report, where the auditor concludes that the financial statements are presented fairly in all material respects and are in accordance with the applicable accounting standards.

- **Qualified opinion:** This type of audit report is issued when the auditor concludes that the financial statements are presented fairly in all material respects except for a specific issue or limitation that is disclosed in the report.
- **Adverse opinion:** This type of audit report is issued when the auditor concludes that the financial statements are not presented fairly in accordance with the applicable accounting standards.
- **Disclaimer of opinion:** This type of audit report is issued when the auditor is unable to form an opinion on the financial statements due to limitations or restrictions on the audit.
- **Other audit reports:** In addition to the above types of audit reports, there may be other types of reports that auditors may issue, such as reports on internal controls or reports on specific aspects of the financial statements.

Sample:

[Company Name]

Auditor's Report

[Date]

To the Shareholders of [Company Name]:

We have audited the financial statements of [Company Name] (the "Company") for the year ended [Year End Date], which comprise the balance sheet, income statement, statement of changes in equity, and cash flow statement, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements:

The Company's management is responsible for the preparation and fair presentation of these financial statements in accordance with [applicable financial reporting framework], and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility:

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with [applicable auditing standards]. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion:

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of [Company Name] as of [Year End Date], and its financial performance and its cash flows for the year then ended in accordance with [applicable financial reporting framework].

[Auditor's Signature]

[Date]