

Quadrant II –Notes and Related Materials

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Unit III Audit Process

Module Name: Audit Notebook - Meaning, Purpose, Content and Benefits

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AUDIT NOTE BOOK

Notes

Meaning

It is a note book maintained by the auditor for recording a large variety of matters observed during the course of audit. It is a part of record of the auditor available for future reference. It contains errors, difficulties, doubtful queries of various accounting records. It is also called as Audit Memoranda. It is a written record of the queries made, replies received there to, correspondence entered into etc.

Structure of Audit Note Book

1. General Information includes the following:

- a) Nature of the business carried on.
- b) Important provisions affecting its functioning such as Memorandum of Association, Articles of Association, Partnership Deed etc.
- c) Structure of the financial and administrative organization.
- d) A list of the books of accounts.

- e) Names of the Principal Officers, their duties and responsibilities.
- f) Particulars of the system of accounts and informal control which are in operation.
- g) Particulars of the accounting and financial policies followed.
- h) Important contracts to which the client is a party e.g. collaboration contracts, Royalty contracts, etc.

2. Current Information

Current information contains the following:

- a) Audit queries not cleared immediately e.g. missing receipts, vouchers etc.
- b) Mistakes or irregularities observed during the course of audit e.g. failure to comply with requirements of the Companies Act, or the provisions of the Memorandum of Association or Articles of Association, a change in the basic of valuation of Finished Stock and work in progress or in computation of depreciation, failure to provide adequate depreciation etc.
- c) Unsatisfactory book keeping arrangements, casting method, internal or financial administration or organisation.
- d) Important information about the company which is not apparent from the accounts.
- e) Special points requiring consideration at the time of verification of final accounts.
- f) Important matters for future reference.

Purpose of Audit Note Book

Audit note book forms an important part of the documentation for the Auditor. The following points indicate its usefulness from different points of view:

1. Evidence Value

In case notes have been properly made in the Audit Note Book, it might prove of great value to the auditor later on. It has an evidence value in case a suit is filed

against him for negligence or misfeasance. Such a note book will be a documentary evidence in favour of the auditor even after several years by which time the auditor might have forgotten everything about that particular audit. The importance of such an Audit Note Book was emphasized by Lord Justice Vaughan Williams in the London and General Bank case. In the same way, the Audit Note Book which contained detailed information was of great assistance to the auditor in the case of the City Equitable Fire Insurance Company.

2. Subsequent Audit Value

The Audit note book should be clear, concise and complete so that it may be quite intelligible to the clerk who audits the accounts of the same company next year. Such a note book can be a useful guide to such a clerk.

3. Planning Value

The Audit note book is quite useful document in planning the next audit of the entity. It is also useful in preparing the next audit programme as the weaknesses shown in the Audit note book on various aspects and segments of accounting would require close follow-up.

4. Protection Value

The audit note book is a comprehensive record of work done and audit observation. Hence, it is extremely valuable to the Auditors as a document of defense when a charge is brought against the Auditor for negligence and other shortcomings in the audit work (for example in the case of Recity Equitable Fire Insurance Company).

5. Control Value

It has also control value as it will show the extent and coverage of work done when the assistants are shifted or when there is a temporary stoppage of work.

6. Audit Process Value

The Audit note book provides new thrusts and direction in the manner, extent and timing of audit checkings.

7. Report finalisation Value

The Audit note book is also very useful at the time of finalising the Audit Report. In the case of follow-up observations made by the Auditor, may get settled with explanation and evidence given by the management at a subsequent stage. After that, the Auditor has to consider only the unsettled observations from various relevant angles for preparing the Audit Report. Thus, Audit note book is the primary basic document in preparing the Audit Report on the true and fair view of the financial statements.

Advantages of Audit Note Book

- 1. Important matters relating to audit work may be easily remembered** - Audit notebook serves as a valuable tool to remember information relating to audit, queries and explanations sought and rendered during the course of audit.
- 2. Ensures continuity of audit work** - Every audit assistant records his observations along with explanations obtained on accounts under audit in the audit notebook. The audit work, as a result, is not affected by the temporary absence of the concerned assistant. The auditor can entrust some other clerk with the work. Thus, the audit notebook ensures continuity.
- 3. Serves as a proof against charge of negligence** - The audit notebook is an important evidence on all the matters considered by the auditor during the course of audit. It can serve as a testimonial against any charge of negligence brought against the auditor by the clients in the court of law. Its evidentiary value has been recognised in many legal

decisions, in particular, in *City Equitable Fire Insurance Co. Ltd. Case* and *London and General Bank case*. It serves as an evidence in the court of law in case of dispute

4. **Serves as a guide in framing future audit programmes** - The assistants write queries and replies thereto in the audit notebook. Such information and explanations may serve as an important reference point for framing future audit programmes.
5. **Easy preparation of audit report** -It facilitates easy preparation of audit report.
6. **Assess efficiency of audit staff** -It helps the auditor in assessment of efficiency of audit staff.