

Overall Objectives of an Independent Auditor: A Cross Country Analysis

Dr. Siddhartha Sankar Saha
Associate Professor of Commerce, Department of Commerce and MBA
University of Calcutta, West Bengal, India

Mitrendu Narayan Roy
Research Scholar, Department of Commerce, University of Calcutta, &
Assistant Professor, Goenka College of Commerce and Business Administration, West Bengal, India

Abstract

Statutory auditors are required to attest material accuracy, appropriateness and fairness about financial statements of corporate enterprise. Quality of their work depends upon their competence and independence towards their profession. Existing auditing standards guides an auditor through the audit procedure. Out of them, there is one standard that set the overall objectives of an independent auditor. The current study makes a comparative analysis of overall objectives of an independent auditor as per their governing standards in USA, UK and India. It is observed that the requirements relating to overall objectives are almost similar in UK and India. However, the standard governing overall objective is more comprehensive in USA.

Keywords: Statutory Audit, USA, UK, India, Overall Objectives.

1. Introduction

A quality financial report guides the stakeholders about financial performance, financial position and future prospect of the business for the purpose of decision making (Saha, 2015) which ultimately protect their interest. In order to maintain quality of financial statements, a competent authority external to the enterprise must verify the authenticity of financial statements with respect to accounting principles and the legal norms. Highly skilled accountants with an affiliation to a professional body are appointed by the shareholders of the corporate enterprise to perform this role. There is no denying to the fact that a quality audit is likely to detect earnings management and assure quality of financial reporting thereby protect stakeholders' interest. Many sections of the stakeholders recognise audited financial statements as free from manipulation and frauds. Thus, auditors are supposed to play a significant role in the economy in protecting stakeholders' interest (Gupta, 2005). However, because of recent corporate accounting scandals, extensive growth in white-collar crime, the ensuing chaos for precision and sincerity in reporting, the accounting professions have been facing challenges as to how quality of audit can be excelled with an ultimate goal of safeguarding stakeholders' interest (Bakshi, 2004). Since financial decision of a large part of the society depends upon auditors' opinion, regulatory authorities in a country enforce certain regulatory pronouncements for the auditors (Brewster, 2003). Professional institute and other regulatory bodies governing statutory audit operations in several countries across the globe have come up with several professional and ethical standards for maintaining quality of statutory audit of financial statement (Francis, 2004).

In most of the developed and developing countries, statutory audit operation is controlled by auditing standards usually issued by the professional institute. Different issues concerning audit procedures are monitored with the help of these standards. However, in the regulatory framework of every country, there is one standard that set the overall framework of statutory audit and defines overall responsibility of statutory auditors. In India, professionally qualified Chartered Accountants (CAs) are supposed to play the role of independent statutory financial auditors. Professional pronouncements, especially Standards on Auditing (SAs) issued by the Institute of Chartered Accountants of India (ICAI) are supposed to guide them in maintaining good faith, integrity, independence and transparency. At present there are 37 SAs dealing with diverse issues concerning statutory financial audit. Out of them, SA-200 titled, '*Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing*' is very important as it set the overall framework for audit and defines the overall objectives of an independent auditor.

The current study is an attempt to comparatively analyse overall objectives of an independent auditor in a few countries including India.

2. Objectives

The main objectives of the study are

- (i) To review the requirements of auditing standards governing overall objectives of an independent auditor in a few countries including India; (Refer to Section 4.1)
- (ii) To make a comparative analysis among a few countries including India based on overall objectives of an independent auditor in the light of governing auditing standards (Refer to Section 4.2).

3. Methodology

To investigate the area under study, at the beginning, an endeavour has been made to look into the accessible literature on overall objectives of an independent auditor in order to gather a conceptual idea on regulatory requirements behind it. Based on this theoretical knowledge, a modest effort has been made to formulate the plan of work to make a comparative study of overall objectives of independent auditor in a few countries.

World Bank, Central Intelligence Agency (CIA) and International Monetary Fund (IMF) ranks all the countries in the world individually in terms of their national Gross Domestic Product (GDP) calculated as per Purchasing Power Parity (PPP) method. In the list published each of these three organisations at the end of 2013, top ten countries have been selected. The United States of America (USA), the United Kingdom (UK), and India are persistently present in the group of first ten countries in each of these lists. Hence, based on Judgemental Sampling technique, these three countries have been selected for comparative analysis. During the period of January 2015 to June 2015, different libraries in Kolkata are visited and several books, journal articles, working papers, legal case decisions and online materials are consulted to gather maximum knowledge about these countries and the legal environment governing overall objectives of an independent auditor there.

4. Overall Objectives of an Independent Auditor: A Comparative Review

Three countries selected in the current paper for comparative analysis of overall objective of an independent auditor have significant contribution to the world GDP. According to the data published by the World Bank, CIA and IMF on country GDPs calculated as per PPP theory, USA was ranked first. A high level of industrial output and corporate growth is one of the important features of this country. It requires USA to have a good regulatory system governing audit practices. Despite having a good regulatory framework, it has witnessed several corporate accounting scandal cases (e.g. Enron, WorldCom) in this country which proves audit failure time and again (Thibodeau & Frier, 2010). The United Kingdom (UK) was ranked 8th in the list of the IMF and the CIA and 9th in the list of the World Bank. Though countries like Japan or Russia was ranked ahead of UK in terms of their GDP, UK is an important member country of the European Union (EU). The concept of global convergence of financial reporting framework and uniformity in statutory audit regulations was first emerged in UK. UK is also the birthplace of the modern corporate governance mechanism with Audit Committee and independent directors in the board. Pioneering role in all these major regulatory aspects, keeps UK ahead of other developing countries in terms of quality of statutory audit of financial statements. Finally, India is the 3rd largest economy in the world as per the list published by World Bank, CIA and IMF. After independence in 1947, India witnessed a constant growth in industrial sector. Presently, Indian service industry is spreading its operations in global market. Growth of corporate sector naturally increases stakeholders' base and accountability of the business towards them. Therefore, with a view to monitoring business practices, Indian financial system has a strong regulatory framework. A strong regulatory framework creates an environment of good audit quality.

In each of the select countries, overall objective of an independent auditor is governed by a particular auditing standard. In USA, the Auditing Standards Board (ASB) under the American Institute of Certified Public Accountants (AICPA) is responsible for issuing auditing standards. Different aspects of auditing which are represented with the help of different Statements of Auditing Standards (SASs) were known as Auditing (AU) sections. With a view to improving the applicability of SASs and making it comparable with International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB) under the International Federation of Accountants (IFAC), ASB has started redrafting the SASs in line with ISAs. Consequently, old auditing (AU) sections were converted into new auditing section. In order to avoid any confusion between the old and new auditing sections, the new auditing sections are termed as Clarified Auditing Sections (AU-C Sections) (Flood, 2015). Overall objectives of an independent auditor and the conduct of an audit in accordance with Generally Accepted Auditing Standards (GAAS) are discussed in this segment. GAAS is represented in the form of SASs and codified using AU-C sections. Overall objectives of an independent auditor are discussed under SAS-122 (AU-C 200) titled, '**Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Generally Accepted Auditing Standards**'. In UK, the Financial Reporting Council (FRC) issued ISA (UK & Ireland)-200 titled, 'Objectives and General Principles Governing an Audit of Financial Statements' that discusses overall objectives of an independent auditor in UK. In India, Overall objectives of an independent auditor are guided under SA-200 (Revised) titled 'Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing' issued by the Institute of Chartered Accountants of India (ICAI).

4.1 Overall Objectives of an Independent Auditor: Conceptual Review

Requirements of the governing auditing standards with respect to overall objectives of an independent auditor are discussed here:

4.1.1 The United States of America

Overall objectives of an independent auditor and the conduct of an audit in accordance with Generally Accepted

Auditing Standards (GAAS) are discussed in this segment. GAAS is represented in the form of SASs and codified using AU–C sections. Overall objectives of an independent auditor are discussed under SAS–122 (AU–C 200) titled, ‘*Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*’. As per this standard, the main objectives of an independent auditor are to collect reasonable assurance that the financial statements is free from material misstatement due to fraud and error and draw their conclusion that financial statements is presented fairly in accordance with applicable financial reporting framework and report on financial statements. The specific requirements of this standard are:

- ◆ The auditor should be independent of the audited entity and should fulfil necessary ethical requirements when performing audit as per Generally Accepted Auditing Standards (GAAS);
- ◆ The auditor should plan and perform audit procedures with professional skepticism;
- ◆ The auditor should exercise professional judgement while planning and performing audit engagement;
- ◆ The auditor should gather sufficient and appropriate evidences to draw reasonable conclusions on financial statements;
- ◆ The auditor should understand clarified auditing (AU–C) sections in details and apply them in conduct of audit. If the auditor did not comply with these sections, they should not mention it in the audited report;
- ◆ The auditor should understand the objectives of each clarified auditing (AU–C) section and decide whether any additional procedures is required to be performed to fulfil a particular objective;
- ◆ The auditor should not refer to clarified auditing (AU–C) section if the section in whole or in part is not relevant for a particular engagement;
- ◆ Requirements under GAAS can be categorised under two groups – unconditional requirement and presumptively mandatory requirement. The auditor is required to fulfil unconditional requirements in all circumstances. However, they may depart from presumptively mandatory requirement. In such cases the auditor should perform alternative audit procedure;
- ◆ The auditor should consider applicable iterative publications while planning and performing audit;
- ◆ The auditor should evaluate the appropriateness of available auditing guidance;
- ◆ If an objective of an AU–C section cannot be fulfilled, the auditor should evaluate its impact on overall objective of the standard. If the overall objective cannot be met, the auditor should withdraw from engagement.

Compliance with requirements of this standard ensures two important elements of audit quality – competence and independence. Professional skepticism and professional judgement also allows an auditor to detect and disclose material misstatement which is an important prerequisite of audit quality. Finally, this standard also requires an auditor to comply with mandatory requirements of other standards under GAAS. Compliance with applicable regulation ensures quality of audit. Hence, this standard basically provides a complete environment for provision of quality audit.

4.1.2 The United Kingdom

Overall objectives of an independent auditor are discussed under ISA (UK & Ireland)–200 titled, ‘*Objectives and General Principles Governing an Audit of Financial Statements*’. Major requirements of this standard are:

- ◆ The auditor should comply with relevant ethical requirement;
- ◆ The auditor should question ambiguous issues in financial statements and recognise circumstances that cause financial statements to be materially misstated;
- ◆ The auditor should apply his competence, skills and experience in taking relevant audit decisions;
- ◆ The auditor should collect sufficient and appropriate evidences to draw reasonable conclusion on financial statements;
- ◆ The auditor should have an understanding of all ISAs (UK & Ireland) and its explanatory materials used in an audit. They should comply with all ISAs (UK & Ireland) and should not report compliance with all ISAs (UK & Ireland) unless they have actually done it;
- ◆ The auditor should plan and perform its audit procedures as per objectives of ISAs (UK & Ireland). The auditor should determine whether any additional procedures is required to be performed beyond those objectives;
- ◆ The auditor may not comply with ISAs (UK & Ireland), if its provisions are not relevant for the audit engagement;
- ◆ If the auditor cannot comply with a particular objective of ISAs (UK & Ireland), it should modify their opinion or withdraw from engagement.

The standard dictates the overall responsibilities of an independent auditor. Compliance with ethical requirement including independence is the basic requirement of a quality audit. Apart from that, this standard also requires an auditor to comply with applicable auditing standards in his audit procedure. A good amount of professional skepticism and professional judgement in an audit engagement will also ensure its quality.

4.1.3 India

Overall objectives of an independent auditor are guided under SA-200 (Revised) titled ‘Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing’ issued by the ICAI. The main responsibilities of the statutory auditors with respect to this standard are:

- ◆ The auditors should comply with pertinent ethical requirements;
- ◆ They should question unclear issues in financial statements and recognise circumstances that cause financial statements to be materially misstated;
- ◆ They should apply capability, skills and knowledge in taking relevant audit decisions;
- ◆ They should collect adequate and suitable evidences to draw reasonable conclusion on financial statements;
- ◆ The auditors should have an understanding of all SAs and its explanatory materials used in an audit. They should fulfil all SAs and should not report compliance with all SAs unless they have actually done it;
- ◆ They should plan and perform its audit procedures as per objectives of SAs. The auditor should decide whether any additional procedures is required to be performed beyond those objectives;
- ◆ They may not comply with SAs, if its provisions are not relevant for the audit engagement;
- ◆ If the auditors cannot comply with a particular purpose of SAs, it should modify their opinion or withdraw from engagement;

The SA-200 (Revised) provides a comprehensive guideline on basic requirement from an auditor to conduct a quality audit. Apart from ethical requirement laid down under Code of Ethics, it also requires an auditor to have a questioning mindset and ability to apply knowledge, skills and experience to identify possibilities of material misstatement without any difficulty. Individual SAs provide guidance to the auditors for performance of a quality audit.

4.2 Overall Objectives of an Independent Auditor: A Comparative Analysis

Requirements of these three standards in three different countries with respect to overall objectives of an independent auditor are projected in Table 1.

Table 1: A Comparative Study on Overall Objectives of an Independent Auditor

Countries	United States of America (USA)	United Kingdom (UK)	India
Parameters			
A. Governing Standard	SA-122 (AU-C 200) titled, ‘Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards’	ISA (UK & Ireland) 200 titled, ‘Objectives and General Principles governing an Audit of Financial Statements	SA-200 titled, ‘Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Standards on Auditing’
B. Requirements	<ul style="list-style-type: none"> ◆ Compliance with relevant ethical requirements; ◆ Professional skepticism; ◆ Professional judgement; ◆ Gathering sufficient and appropriate audit evidence; ◆ Understanding each clarified auditing (AU-C) sections; ◆ Planning audit procedures as per the objective; ◆ Compliance with other standards; ◆ Consideration of iterative publications; ◆ Evaluation of auditing guidance; ◆ Disclosure of non-compliance with an objective with reasons thereof. 	<ul style="list-style-type: none"> ◆ Observance with relevant ethical requirements; ◆ Professional skepticism; ◆ Professional judgement; ◆ Obtaining sufficient and appropriate audit evidence; ◆ Understanding ISAs; ◆ Preparation of audit procedures as per the objective; ◆ Not complying with the standard if it is not relevant; ◆ Modifying opinion in case of non-compliance. 	<ul style="list-style-type: none"> ◆ Conformity with relevant ethical requirements; ◆ Professional skepticism; ◆ Professional judgement; ◆ Collecting sufficient and appropriate audit evidence; ◆ Understanding each SA; ◆ Planning audit procedure as per the objective; ◆ Not complying with the standard if it is not relevant; ◆ Changing opinion in case of non-compliance.

The title of the individual standards in three countries is different. As per the provision of these standards, in all three countries, the statutory auditor is required to comply with relevant ethical requirement. They should exercise professional skepticism and professional judgement and collect sufficient and appropriate evidences to form their conclusion on the financial statements. The auditor should also have a clear

understanding about the standard and should plan their procedure as per its objective. In UK and India, if the auditing standard is not relevant in a particular situation, the auditor may not refer to its provision. The auditor needs to modify their opinion, if they fail to comply with relevant provisions of the standard. In USA, however, there are some other provisions that must be complied with. Compliance with other standards, consideration of iterative publications and auditing guidance while performing audit procedures, disclosure of non-compliance with any particular standard are the requirements of SAS-122 (AU-C 200) in USA.

5. Conclusions

Quality audit of financial statements performed by the statutory auditors ensures reliability and authenticity of financial statements in safeguarding stakeholders' interest. In this perilous time when repeated corporate frauds are deteriorating investors' faith in corporate integrity, it has become more important to ensure fulfilment of overall objectives of an independent auditor. Regulatory frameworks of USA, UK and India have a specific auditing standard to deal with this issue. While the basic requirements of the standards are almost same in select three countries, there are some inherent differences among them. Standards of UK and India are almost similar. However, the standard in the USA is more comprehensive than that of UK and India.

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