



CA FINAL



**HANDWRITTEN NOTES
ADVANCED AUDITING**

For MAY 24 & onwards

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CHAPTER - 5

AUDIT EVIDENCE

★ Overview of Chapter :

▶ Standards which are covered in this Chapter :-

- SA 500 : Audit Evidence
- SA 501 : Audit Evidence - Specific Considerations for Selected items
- SA 505 : External Confirmation
- SA 510 : Initial Audit Engagements - Opening Balances
- SA 530 : Audit Sampling
- SA 550 : Related Parties

SA 500 : Audit Evidence

Concept 1 : Introduction to SA 500 & Audit Evidence

Concept 2 : Scope of SA & Objective of Auditor

Concept 3 : Audit Procedures to obtain audit Evidence.

Concept 4 : Methods in Compliance & Substantive Procedures

Concept 5 : Reliability of info. produced by Mgt. Expert

Concept 1 Introduction to SA & Audit Evidence

SA 500 deals with auditor's responsibility to design and perform audit procedures to obtain SAAE to be able to draw reasonable conclusions on which to base auditor's opinion.

Audit Evidence : It is info. used by auditor in arriving at conclusions on which auditor's opinion is based. It includes

- ↳ Info. in a/c records of FS
- ↳ other info.

Concept 2 Scope of SA and Objective of Auditor

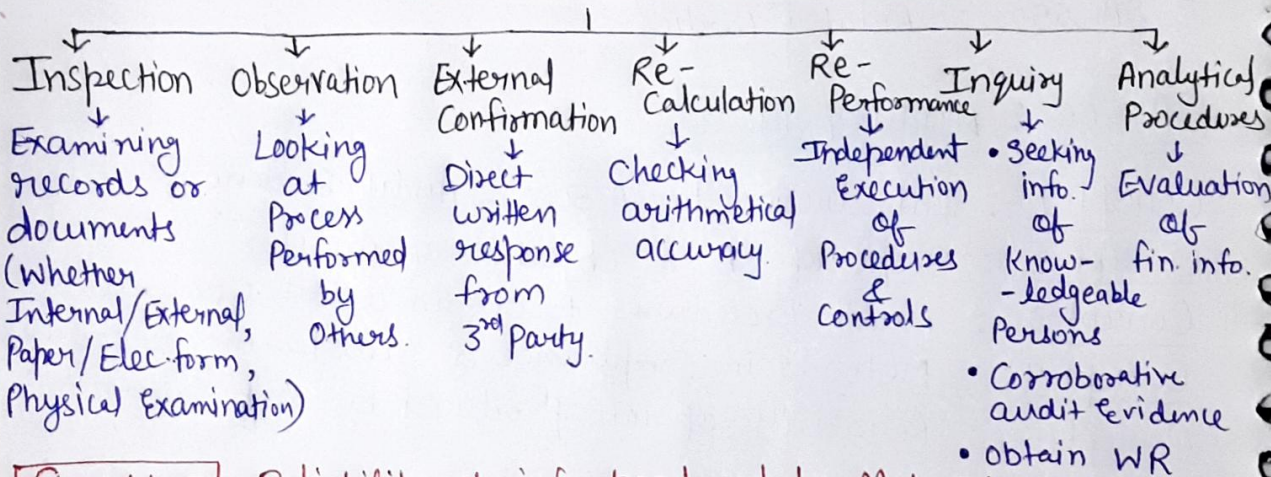
Scope: This SA is applicable to all audit evidence obtained during the course of audit.

Objective: To design & Perform audit procedures to obtain SAAE to be able to draw reasonable conclusions for auditor's opinion.

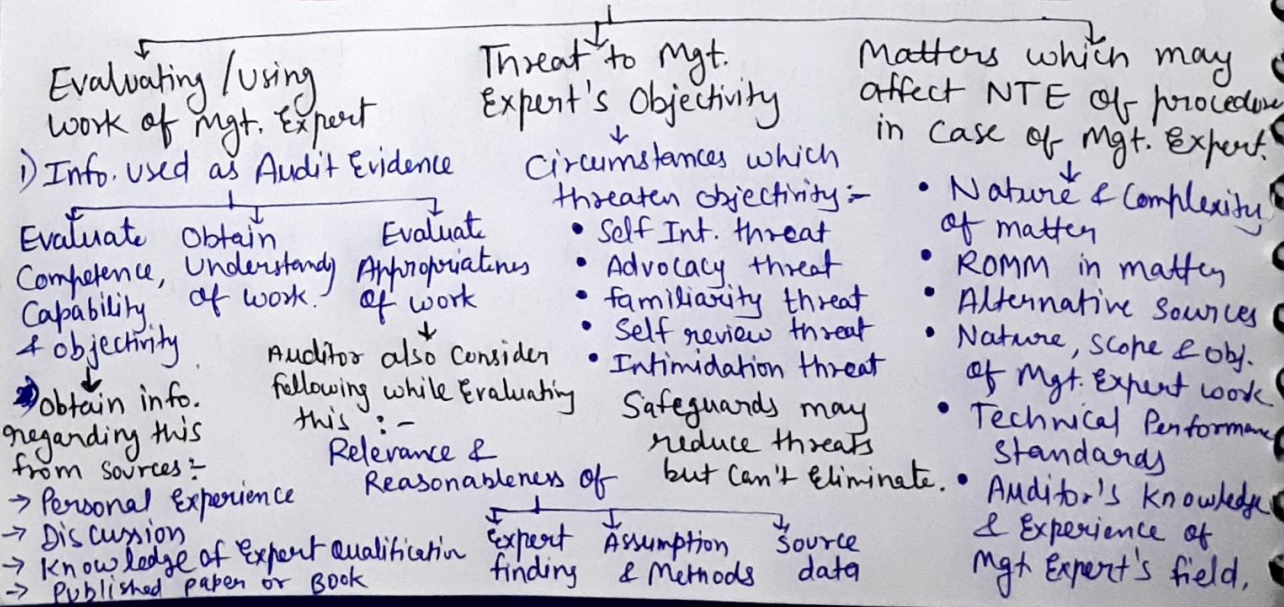
Concept 3 Audit Procedures to obtain Audit Evidence

- (i) Risk Assessment Procedures
- (ii) Further Audit Procedures
 - Compliance procedures (Test of control)
 - Substantive Procedures (Test of details)

Concept 4 Methods in Substantive & Compliance Procedures



Concept 5 Reliability of info. produced by Mgt. Expert



SA 501 : Audit Evidence - Specific Consideration for Selected Items

Concept 1 : Scope of SA & Objective of Auditor

Concept 2 : Special Consideration for Inventory

Concept 3 : Special Consideration for litigations & claims

Concept 4 : Special Consideration for Segment Information

Concept 1 Scope of SA & Objective of Auditor

Scope : This SA deals with specific considerations by auditor in obtaining SAAE with respect to Inventory, Litigations & Claims, and Segment informations in audit of FS.

Objective : To obtain SAAE regarding :-

Existence & Condition
of Inventory

Completeness of
Litigations & claims
involving entity.

Presentation & Dislo-
-sure of segment
info. in accordance
with FRF.

Concept 2 Special Consideration for Inventory

If Inventory is Material, then obtain evidence for Existence & Condition of inventory by :

- Attendance at physical inventory counting
- Performing audit procedures over entity's final inventory records.

If Inventory counting conducted at date other than date of FS

↓

Perform additional procedures b/w count date & date of FS with respect to inventory.

If Auditor is unable to attend physical inventory counting due to unforeseen circumstances

↓

Auditor should make/observe some physical count on alternate date & perform audit procedures on intervening txn.

If attendance at physical inventory count is impracticable.

↓

Auditor should perform alternate procedures

↓

If it is not possible to do so

↓

modify the opinion.

When Inventory is under custody of 3rd Party

↓

→ Request Confirmation from 3rd party

→ Perform inspection & other procedures.

Concept 3 Special Considerations for Litigations & claims

(a) Auditor to perform audit procedures to identify litigations & claims by :-

- 1) Inquiry of Mgt. 2) Reviewing Minutes of meeting 3) Reviewing Legal Expense A/c

(b) If Auditor assesses ROMM \rightarrow Seek direct communication with Entity's External legal Counsel.

Modify the opinion as per SA 705

\leftarrow If Auditor is unable to Communicate

(c) Obtain WR that all known actual or possible litigations & claims have been disclosed to auditor & appropriately accounted as per applicable FRF.

Concept 4 Special Consideration for Segment Information

Auditor to obtain audit Evidence regarding Presentation & Disclosure of Segment info. in accordance with FRF by :-

Understanding the Methods Used by Mgt. in determining Segment info.

Performing Analytical Procedures.

SA 505 : External ConfirmationsConcept 1 : Scope of SA & Objective of AuditorConcept 2 : External Confirmation ProceduresConcept 3 : Mgt.'s refusal to allow auditor to send a confirmation requestConcept 4 : Results of External Confirmation ProceduresConcept 5 : Some Important DefinitionsConcept 1 Scope of SA & objective of AuditorScope : This SA deals with auditor's use of External Confirmation procedures to obtain audit Evidence.Objective : To design & Perform External Confirmation procedure to obtain relevant and reliable audit Evidence.Concept 2 External Confirmation Procedures↓
Determining the information to be confirmed or requested.↓
Selecting the appropriate confirming party.↓
Designing the Confirmation request.↓
Sending the request and also follow-up request.★ Factors which assist auditor in determining whether External Confirmation procedures are to be performed as Substantive audit procedures :-

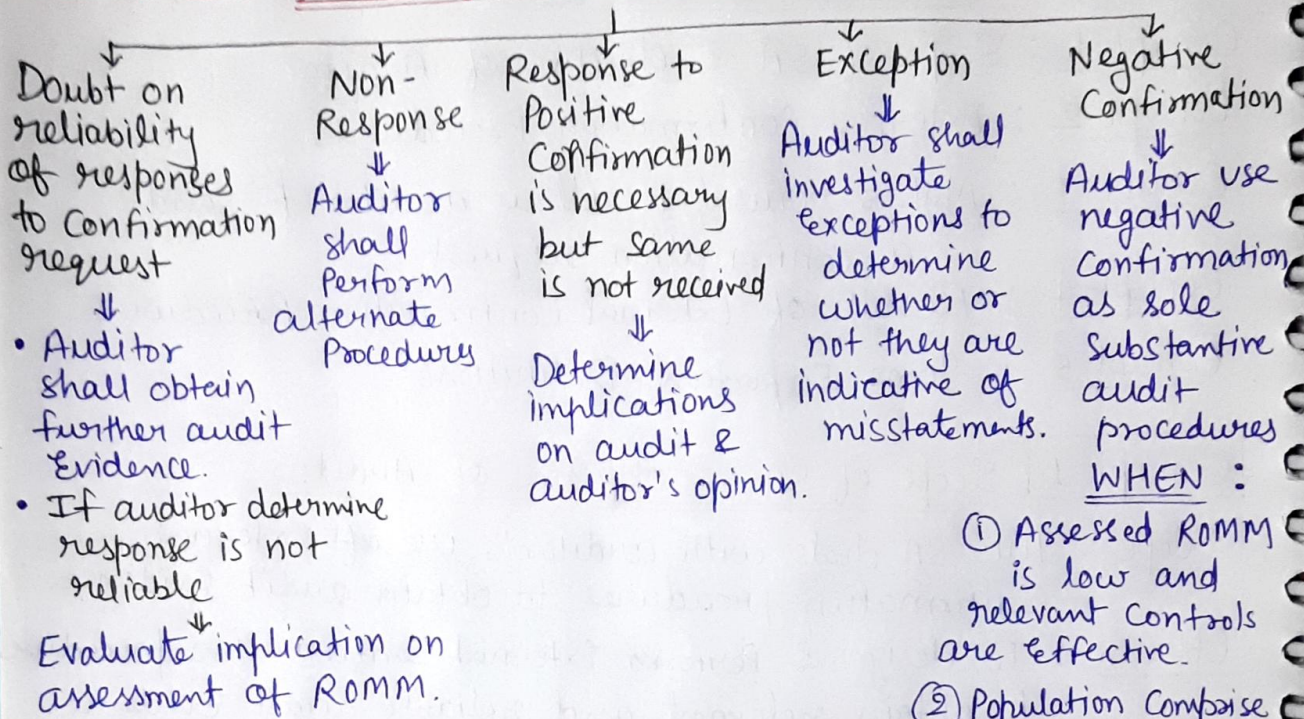
- Confirming party's knowledge
- Ability or willingness to respond
- Objectivity of confirming party

Concept 3 Mgt.'s refusal to allow auditor to send Confirmation request

If Mgt. refuses, then Auditor shall :

↓
Inquire with Mgt. for reasons of refusal. Seek audit Evidence as to their validity & reasonableness.↓
Evaluate the implication of refusal on auditor's assessment of ROMM including risk of fraud & on NTE of other audit Procedures.↓
Perform alternative audit procedures designed to obtain relevant & reliable audit Evidence.↓
If refusal is unreasonable
↓
Communicate with TCWG & Modify report.

Concept 4 Result of External Confirmation Procedures



Concept 5 Some Imp. Definitions

External Confirmations : Direct written response from 3rd party.

Positive Confirmation request : Confirming party respond directly to auditor indicating whether Confirming party agrees or disagrees.

Negative Confirmation request : Confirming party respond directly to auditor only if Confirming party disagrees.

Exception : Response that indicates difference b/w info. requested by auditor and info. provided by Confirming party.

★ Situations where External Confirmation can be used :-

- Bank Balance from Bankers
- A/c receivable Balances
- A/c Payable Balances
- Inventories/Title deeds held by 3rd Party.
- Loan from lenders
- Long O/S share application money.

SA 510 : Initial Audit Engagements - Opening Balances

Concept 1 : Scope of audit & Objective of auditor

Concept 2 : Audit procedures, Audit Conclusion & Reporting

Concept 1 Scope of Audit & Objective of Auditor

Scope : This SA deals with auditors responsibilities relating to opening balances when conducting an initial audit engagement.

Objective : To obtain SAAE about :

→ Whether opening balances contain misstatements that materially affect current period's FS.

→ Whether appropriate alcing policies are consistently applied.

If any changes, then properly accounted for, presented & disclosed.

Concept 2 Audit Procedures, Conclusion & Reporting

Opening Balances

Auditor shall :

- 1) Read most recent FS & predecessor's audit report.
- 2) Determine whether prior period's closing balance correctly B/F.
- 3) Determine opening balances reflect appropriate alcing policies.
- 4) Perform audit procedures
- 5) If current period FS misstated due to misstat. in opening Bal. → Then Communicate with Mgt. or TCWG.

Unable to obtain evidence

↓
Qualified/Disclaimer

Op. Bal. Contains misstated, not properly presented / disclosed

↓
Qualified / Adverse opinion.

Consistency of Alcing Policies

Obtain audit evidence whether alcing policies are consistently applied

↓
If any changes then properly accounted for, presented & disclosed.

↓
If not consistently applied / presented / disclosed

↓
Qualified / Adverse opinion.

Relevant Info. in predecessor auditor's report

If modification in predecessor's audit report, then evaluate effect of matter rise to such modification with respect to current period FS

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If modification is relevant & material to current period FS

↓
Auditor shall modify current period audit report.

SA 530 : Audit SamplingConcept 1 : Scope and objectiveConcept 2 : DefinitionsConcept 3 : Types of Sampling RiskConcept 4 : Sample selection methodsConcept 5 : Sample design, size & selection of items for TestingConcept 6 : Performing Audit Procedures.Concept 7 : Other ConsiderationsConcept 8 : Evaluating results of SampleConcept 9 : Factors affecting sample sizeConcept 10 : Factors determining extent of checking on Sampling plan.Concept 1 / Scope and objective.

Scope : This SA applies when the auditor has decided to use audit sampling in performing audit procedures. It deals with auditor's use of

→ Statistical sampling
→ Non-statistical sampling

Objective : To provide a reasonable basis for auditor to draw conclusions about population from which sample is selected.

Concept 2 / Definitions

Audit Sampling : Application of audit procedures to less than 100% of items within population of audit such that all the sampling units have a chance of selection in order to provide auditor with a reasonable basis on which to draw conclusion about entire population.

Tolerable Misstatements : Monetary Amt. set by auditor is not exceeded by actual misstatement. while designing a sample, auditor determine tolerable misst. to address risk that aggregate of individually immaterial misst. may cause FS to be materially misstated.

Concept 3 | Types of Sampling Risk

Sampling Risk : It is risk that auditor's conclusion based on sample may be different from conclusion if entire population were subjected to same audit procedures.

(Total checking ka conclusion sample ke conclusion se alag hona is sampling risk)

It leads to 2 types of Erroneous Conclusions

In case of Test of Control
Control more effective है ऐसा मान लिया जबकि Actual में नहीं है।

In case of Test of details
Material misstat. नहीं है ऐसा मान लिया जबकि Misstat. Exist करते हैं।

Sampling से ये Erroneous Conclusion का risk रहता है which affects Audit Effectiveness and leads to Inappropriate audit opinion.

(चीजे खराब है & अच्छी दिखा दी तो audit effective नहीं होगी & opinion गलत होगा।)

In case of Test of Control
Control less effective है ऐसा मान लिया जबकि actual में Effective है।

In case of Test of details
Material misstat. Exist करते हैं ऐसा मान लिया जबकि Exist नहीं करते हैं।

Sampling से ये Erroneous Conclusion का भी risk रहता है which affects audit efficiency as it leads to additional work to establish that conclusion were incorrect.

(चीजे अच्छी है & खराब दिखा दी तो efficiency नहीं आएगी bcoz additional मेहनत करनी पड़ेगी।)

Concept 4 | Sample Selection Methods

Random Selection

Applied through random NO. generators

Systematic Selection

No. of sample units is divided by Sample size

Monetary unit Sampling

Value weighted selection where size, selection & evaluation in monetary amounts.

Haphazard Selection

Sampling without following structured Techniques.

Block Selection

Selection of blocks. This Tech. can not ordinarily used.

Concept 8 | Evaluating Results of Audit Sampling

Auditor shall evaluate -

- a) Result of Sample and
- b) whether use of audit sampling has provided reasonable basis for conclusions about population tested.

In case auditor concludes that audit sampling has not provided a reasonable basis for conclusions about population tested, Auditor may request mgt. -

- To investigate misstatements identified and potential for further misstatements.
- To make any necessary adjustments OR NTE of those further audit procedures to best achieve required assurance.

Concept 9 | Factors affecting Sample Size

Test of Controls		Test of Details	
<u>Situation</u>	<u>sample size</u>	<u>Situation</u>	<u>Sample size</u>
1) Increase in extent to which auditor's risk assessment takes relevant control	Increase	1) Increase in auditor's assessment of ROMM	Increase
2) ↑ in tolerable rate of deviation	Decrease	2) ↑ in use of other substantive procedures directed at same assertion	Decrease
3) ↑ in expected rate of deviation of population to be tested.	Increase	3) ↑ in auditor's desired level of assurance	Increase
4) ↑ in auditor's desired level of assurance	Increase	4) ↑ in tolerable misstat.	Decrease
5) ↑ in no. of sampling units in population.	Negligible effect.	5) ↑ in amount of misstat. auditor expects to find in population.	Increase
		6) stratification of population.	Decrease

Concept 10 | Factors determining Extent of checking on Sampling plan

Size of Organisation	State of Internal Control	Adequacy & Reliability of Books & Records	Tolerable Error range	Degree of desired Confidence
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SA 550 : Related PartiesConcept 1 : Scope of SA & objective of AuditorConcept 2 : Related partyConcept 3 : Requisition of SAConcept 4 : Identification of previously unidentified/undisclosed related party transactionsConcept 5 : Identified significant related party txn. Outstanding the Entity's Normal Course of business.Concept 6 : Obtain written representationConcept 7 : Communication with TCWGConcept 8 : DocumentationConcept 1 Scope of SA and objective of AuditorScope : This SA deals with auditor's responsibilities regarding related party relationships & transactions.

It Expands on how SA 315, 330, 240 are to be applied in relation to related party relationship & txn.

Objective : To obtain an understanding of related party txn. to:

To recognize fraud risk factors arising from such transactions

To conclude whether FS in so far as they are affected by such transactions -

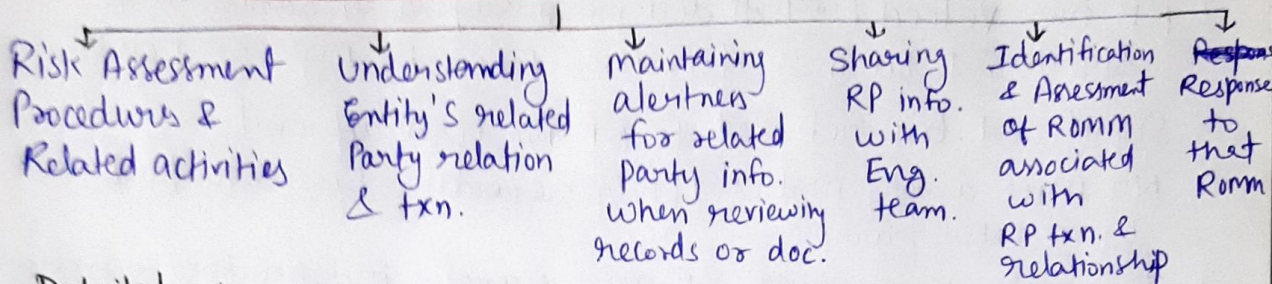
- Achieve true & fair presentation.
- Not misleading.

To obtain audit evidence as to whether related party txn. are properly identified, accounted for and disclosed in FS.

Concept 2 Related PartyA party that is either related party as defined in FRF or where FRF establish minimum or no related party requirements:

- Person or reporting Entity has control / Significant influence → over reporting Entity.
- Another Entity जिस पर reporting Entity का Control/sig. influence है
- Another Entity & reporting Entity Common Control में है through Common Controlling ownership, close family members, or common key mgt.

Concept 3 Requirement of SA



Detailed Discussion of some of above or other points :-

★ Understanding Entity's related party relationship & transaction

Auditor shall inquire of Mgt. regarding -

- Identity of Entity's Related party
- Nature of relationship
- Type & purpose of txn.

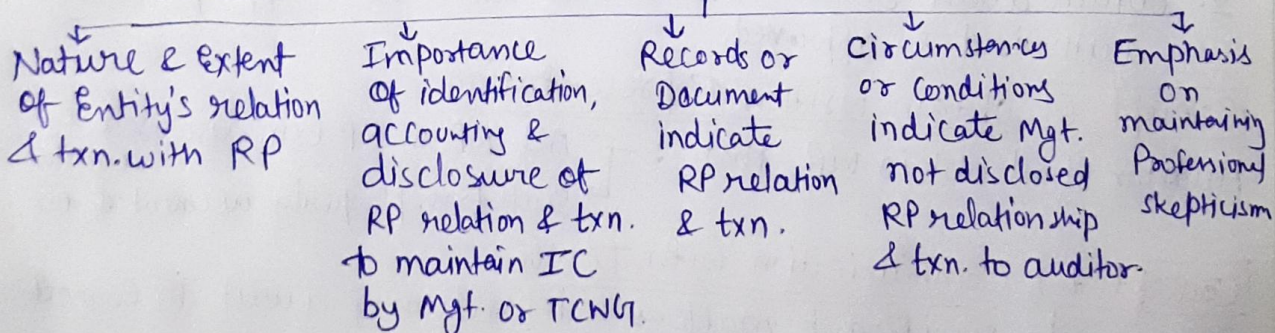
★ Maintaining alertness for related party info. when reviewing records or documents

Auditor shall remain alert when inspecting records or documents for info. that indicate existence of related party relationship or transactions that Mgt. has not previously identified or disclosed to auditor.

For this purpose, auditor shall inspect following :

- Bank, legal & third party confirmation obtained by procedures.
- Minutes of meeting
- Other records or documents as necessary.

★ Eng. Team Discussion : Matter include -

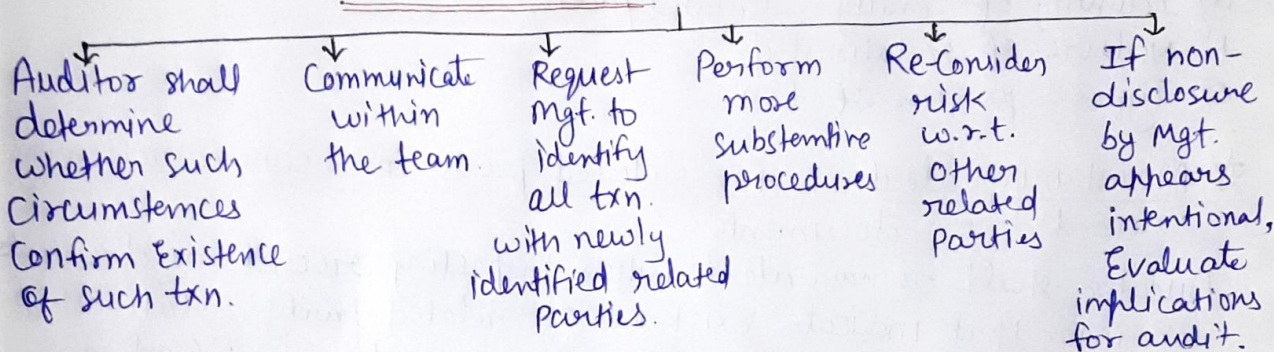


★ Fraud Risk factors : Domination of Mgt. by single person or small group of persons without compensating controls is a fraud risk factor.

Indicators of dominant influence by related party include-

- RP has vetoed (किरी) or decision to suspend या cancel करना Significant business decisions taken by Mgt. or TCWG.
- Significant txn. referred to RP for final approval.
- No issue among Mgt. & TCWG regarding business proposals by Related party.
- Transactions involving RP are rarely independently reviewed and approved.

Concept 4 Identification of Previously unidentified/undisclosed RP transactions



Concept 5 Identified significant RP transactions outside the Entity's normal course of business

1. Inspect underlying Contracts & Evaluate :
 - Business rationale of transactions
 - Whether terms of txn. are consistent with Mgt.'s explanations.
 - Whether such txn. properly accounted.
2. Obtain audit evidence that txn. have been appropriately authorised & approved.

Concept 6 Obtain written Representation

Auditor shall obtain WR that : → All RP & RP txn. disclosed to auditor.
→ Such txn. properly accounted for.

Concept 7 Communication with TCWG

Communicate significant matters arising during audit in connection with Entity's related parties.

Concept 8 Documentation

Auditor shall include Names of related parties & Nature of related Party transactions.