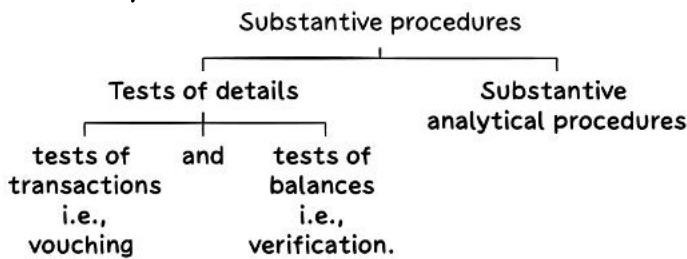
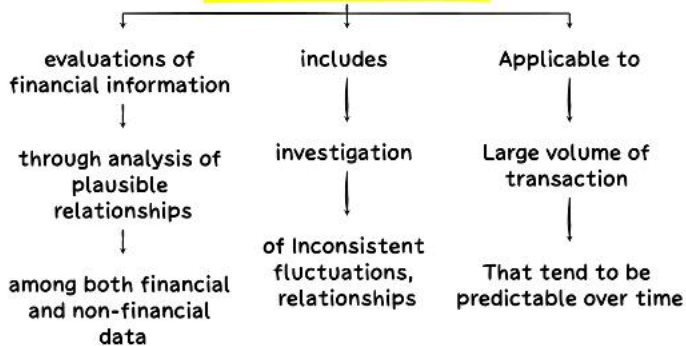


Substantive procedures



Analytical Procedures



- **Payroll Cost:**
 - Fixed employee count and pay rates allow accurate payroll cost estimation.
 - Provides audit evidence, reducing the need for detailed payroll testing.
- **Hotel Room Rental Income:**
 - Analytical procedures predict total rental income using tariff rates, room count, and vacancy rates.
 - If verified, it provides strong evidence, reducing detailed testing.

Designing and Performing Substantive Procedures

Irrespective of the assessed ROMM, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure.

Depending on the circumstances, the auditor may determine that

1. Performing only substantive analytical procedures will be sufficient to reduce audit risk to an acceptably low level. For example, where the auditor's assessment of risk is supported by audit evidence from tests of controls.
2. Only tests of details are appropriate.
3. A combination of substantive analytical procedures and tests of details are most responsive to the assessed risks.

Example: A company has strong internal controls over revenue recognition, tested and found effective by the auditor.

Substantive Analytical Procedure: Auditor analyzes monthly revenue trends against past periods and industry benchmarks.

Conclusion: If fluctuations align with expectations and no anomalies are found, detailed transaction testing may not be needed, reducing audit risk to an acceptably low level.

The nature of the risk and assertion is relevant to the design of tests of details.

1. For example, tests of details related to the existence or occurrence assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence.
2. On the other hand, tests of details related to the completeness assertion may involve selecting from items that are expected to be included in the relevant financial statement amount and investigating whether they are included.

Existence or Occurrence Assertion

- **Risk:** ABC Ltd. might have overstated accounts payable by recording liabilities that do not exist.
- **Test of Details:** The auditor selects items from the accounts payable ledger and verifies them against supplier invoices, purchase orders, and goods receipt notes.
 - ✓ **Example:** If ABC Ltd. recorded a ₹5 lakh payable to a supplier, but no invoice or delivery exists, it indicates an overstatement.

Completeness Assertion

- **Risk:** ABC Ltd. might have understated accounts payable by omitting liabilities.
- **Test of Details:** The auditor selects invoices from major suppliers and checks if they are properly recorded in the accounts payable ledger.
 - ✓ **Example:** If ABC Ltd. received goods worth ₹3 lakh in March but failed to record the liability, it indicates an understatement.

Substantive procedures and results of Test of control

Because the assessment of the risk of material misstatement takes account of internal control, the extent of substantive procedures may need to be increased when the results from test of controls are unsatisfactory.

Extent of testing in Test of details

In designing tests of details, the extent of testing is ordinarily thought of in terms of the sample size. However, other matters are also relevant, including whether it is more effective to use other selective means of testing.

Selective Testing Methods: Instead of increasing sample size, auditors use effective techniques.

Targeted Testing

- Focus on high-risk transactions.
- **Example:** Check high-value inventory (laptops, mobiles) prone to theft.

Data Analytics & Stratification:

- **Concept:** Use technology to find unusual transactions.
- **Example:** Identify slow-moving inventory that may be overstated.

Internal Financial Controls as per Regulatory Requirements Meaning

The term Internal Financial Controls (IFC) basically refers to the policies and procedures put in place by companies for ensuring:

- Reliability of financial reporting
- Effectiveness and efficiency of operations
- Compliance with applicable laws and regulations
- Safeguarding of assets
- Prevention and detection of frauds

Reporting Requirements

Relevant provision of Companies Act, 2013	Nature of Responsibility
Section 134 (5)(e)	In case of Listed Companies , the Directors' responsibility statement shall state that <ul style="list-style-type: none"> ● the Directors had laid down Internal financial controls to be followed by the company and ● that such Internal financial controls are adequate and were operating effectively.
Section 143(3)(i)	The auditor's report shall state whether the company has adequate Internal financial controls system in place and also on the operating effectiveness of such controls. This requirement shall not apply to a private company which - <ul style="list-style-type: none"> i) is One Person Company or a small company; or ii) has turnover less than ₹ 50 crore as per latest audited FSs; and which has aggregate borrowings from banks or financial institutions or any body corporate at any point of time during the financial Year for less than ₹ 25 crore
Section 177(4)(vii)	Every audit Committee shall act in accordance with the terms of reference specified in writing by the Board which shall, inter alia, include - evaluation of IFC and risk management systems
Section 149(8)	Company & independent directors must follow Schedule IV (Code of Ethics). Role of Independent Directors as per code satisfy themselves on <ul style="list-style-type: none"> ● integrity of financial information. ● financial controls and the systems of risk management are robust and defensible.

The directors and management have **primary responsibility** of implementing and maintaining an effective internal controls framework and **auditors** are **expected** to **evaluate, validate** and **report** on the **design** and **operating effectiveness** of **internal financial controls**.

Documenting Risk		
Auditor shall document	Discussion and Decisions	Engagement team discussions and key decisions.
	Understanding	Entity, environment, internal controls, sources, and procedures.
	Risk Assessment	Identified risks at financial statement & assertion levels.
	Controls	Risks and related controls understood by the auditor.