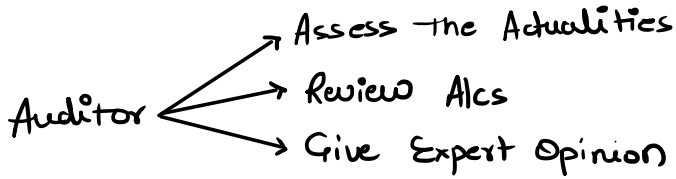


\* 1.1 - Introduction

Auditing → Logical Process



Not possible  
 ↓  
 unless  
 ↓  
 F. s. → Examined → Objectively



To assess

How far FS present

Actual state of affairs

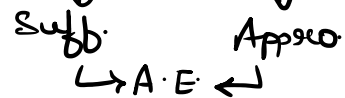
FS present

Trust & Fair view

\* SA 500 → Objective of the Auditor → Design & Perform → Audit Procedures

As to enable the Auditor

To obtain



To draw Reasonable Conclusion

To base the Auditor's Opinion

1.2 - Meaning of Audit Evidence as per SA 500

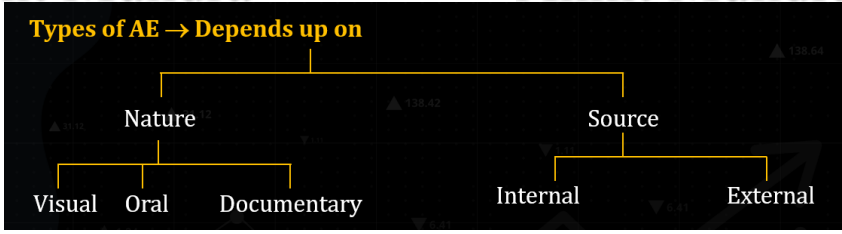
**Audit Evidence (A.E.)**

Info. Used by the Auditor → In arriving at conclusion → on which → Auditor's opinion is based

Contained in the Records

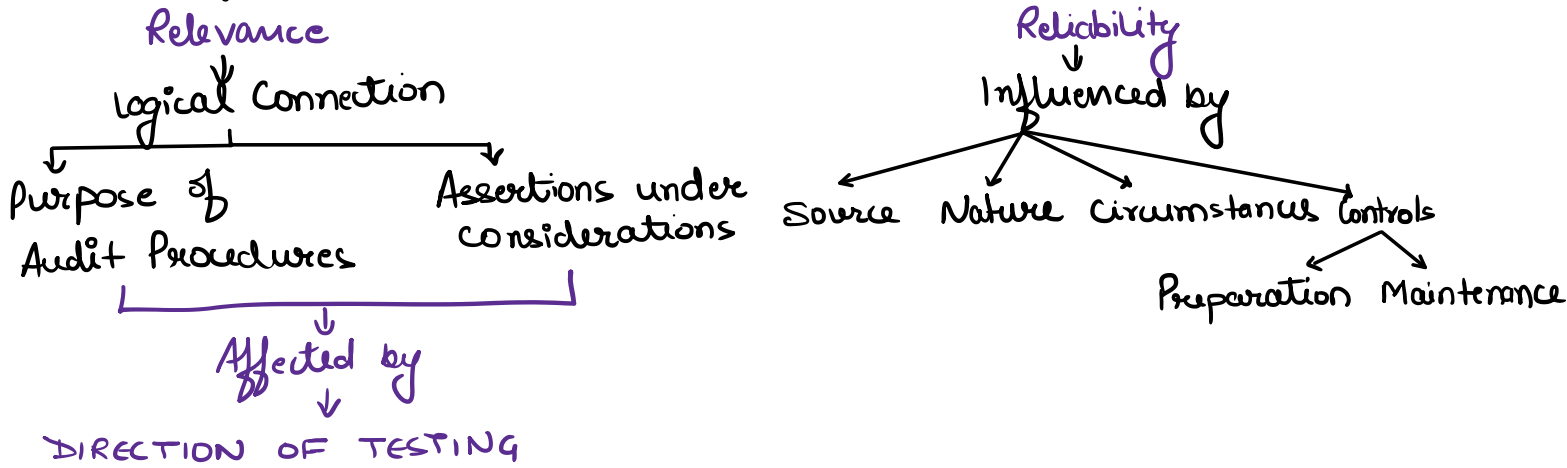
Other Info. (Member of Meetings. Written Confirmation, etc.)

1.3 - Types of Audit Evidence

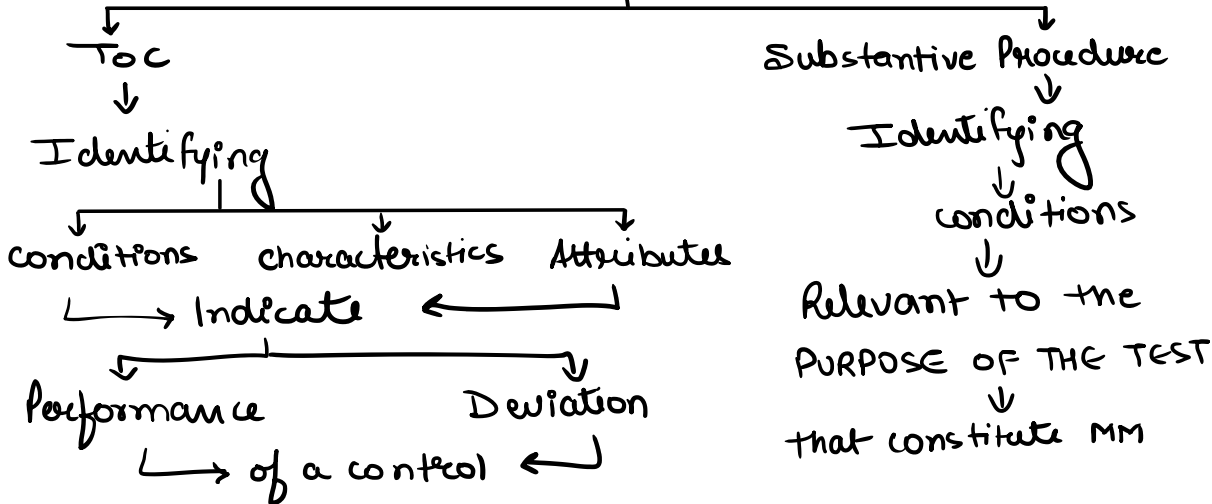


1.4 - Relevance and Reliability of audit evidence

Quality of an Audit → Affected by

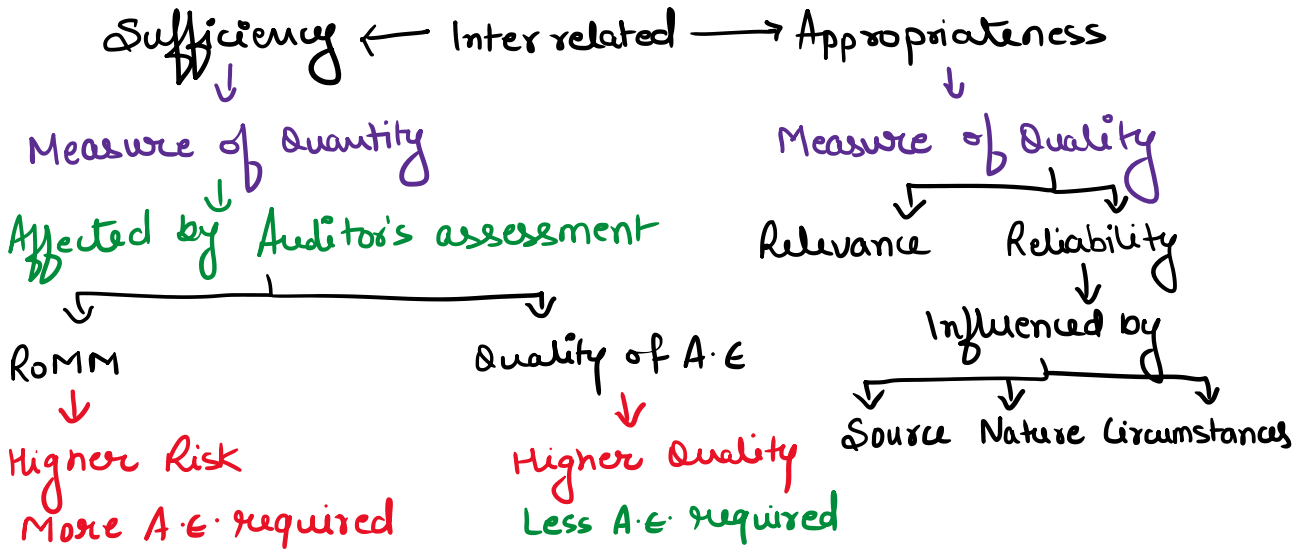


\* Relevant A.E. in Designing

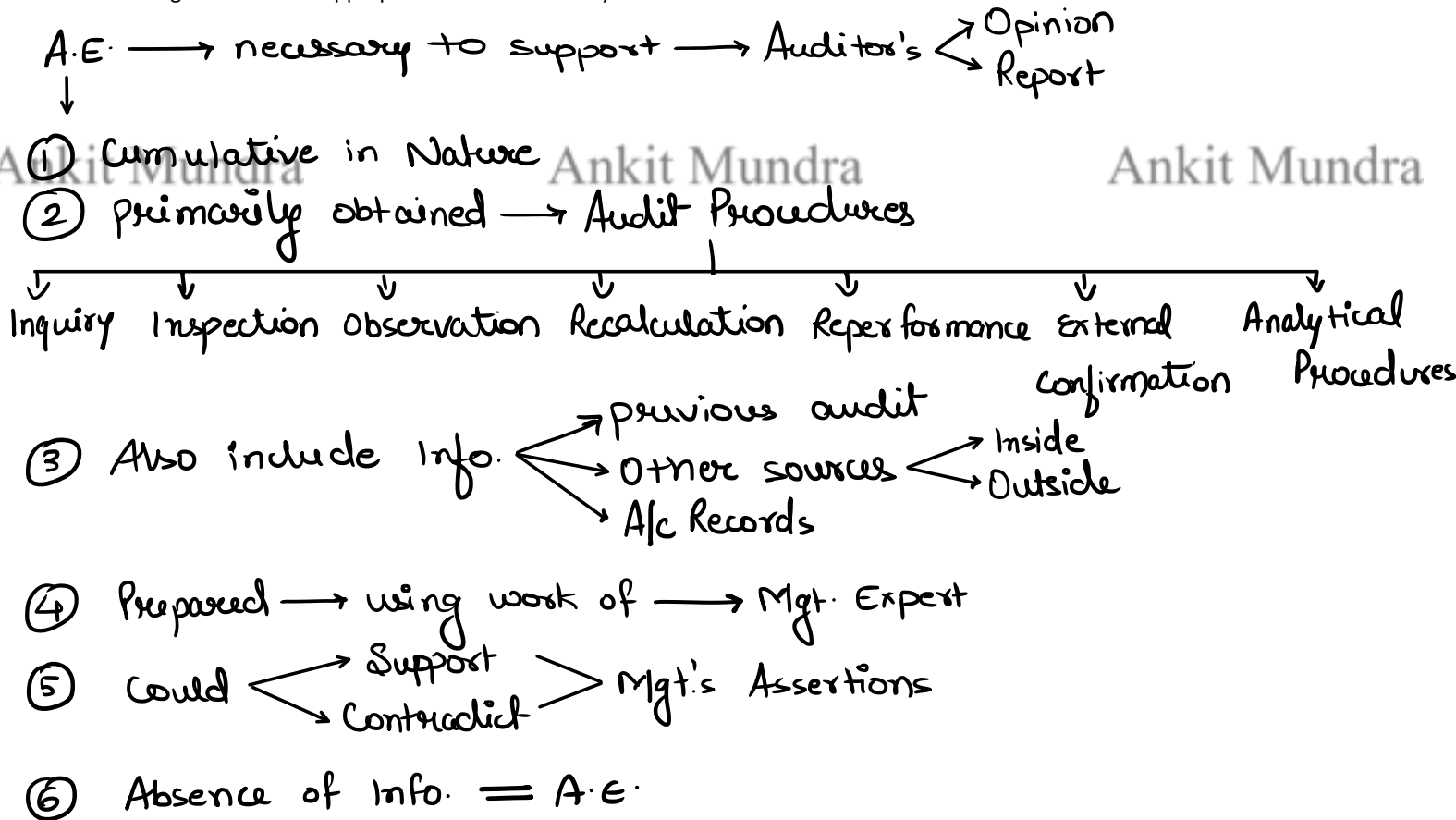


1.5 - Sufficient appropriate audit evidence

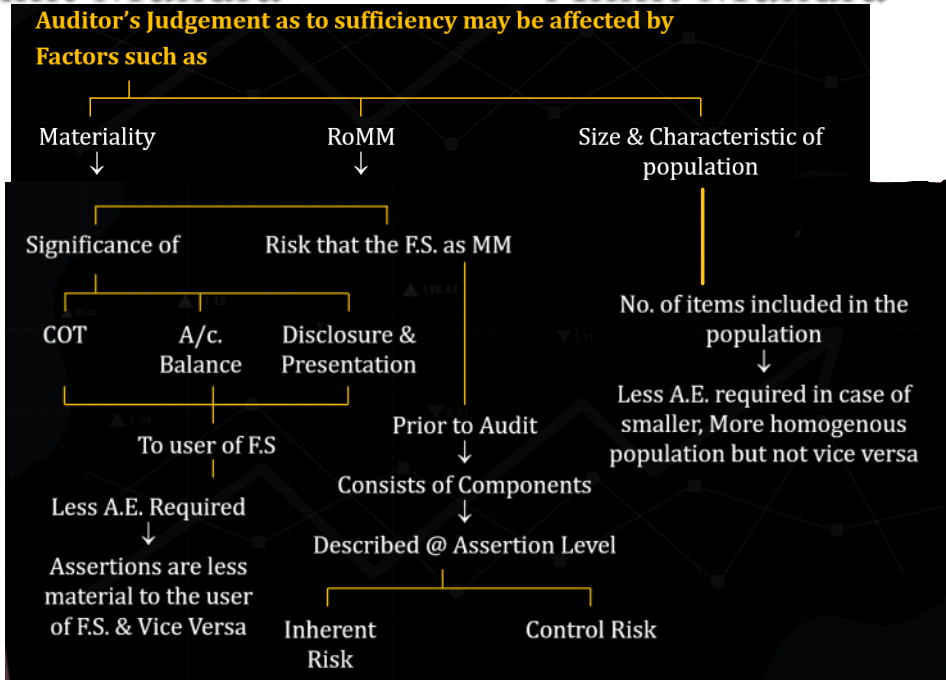
1.5.1 - Sufficiency and Appropriateness are interrelated



1.5.2 Obtaining Sufficient and appropriate Audit Evidence by the Auditor

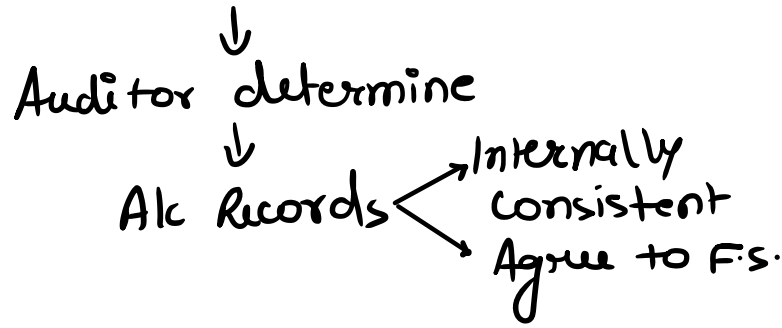


1.5.3 - Further, auditor's judgement as to sufficiency may be affected by the factors such as:



1.6 - Source of audit evidence

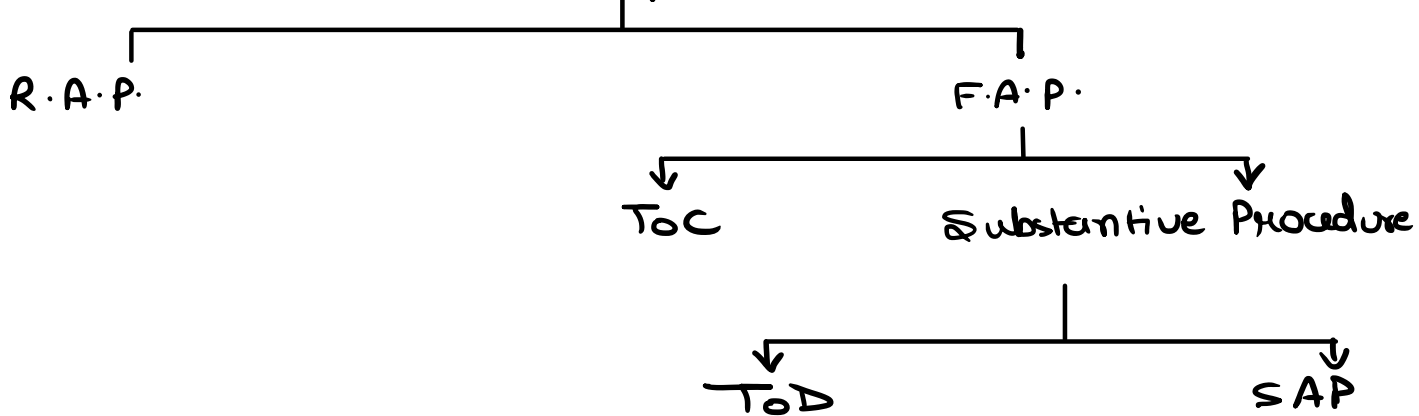
Some A.E. → obtained by → Audit Procedures → A/c Records



More Assurance → Consistent A.E. → Different → Source Nature

## 1.7 - Audit procedures for obtaining audit evidence

A.E. → obtained by performing

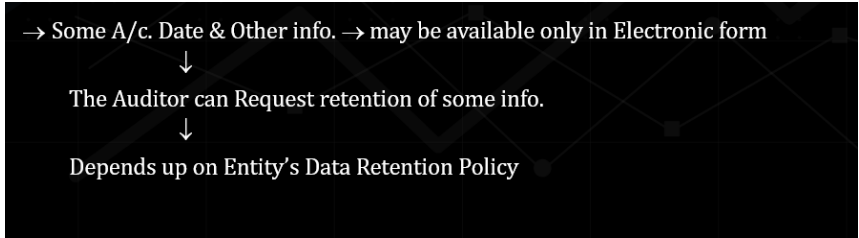


## 1.7.1 - Audit procedures to obtain audit evidence can include:

- i) Inquiry → seeking info. → knowledgeable person
  - Inside
  - Outside
- ii) Inspection → Examining → Records Docs.
- iii) Observation → Looking at → Process procedure
- iv) Recalculation → Mathematical accuracy
- v) Reperformance → Independent execution → procedures controls
- vi) External Confirmation → Direct written Response
  - ↓
  - To Auditor → from 3<sup>rd</sup> Party
- vii) Analytical Procedure → Evaluation → Financial info.
  - ↓
  - Study of plausible relationship
  - Financial Non financial
  - ↳ Data



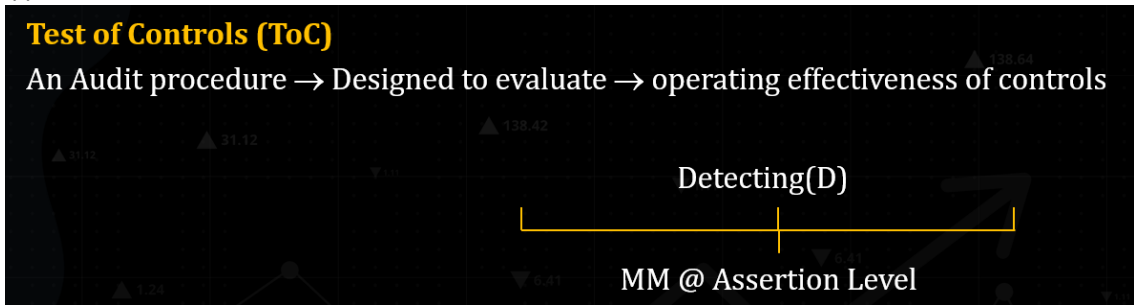
1.7.3 - Nature and Timing of the Audit Procedures



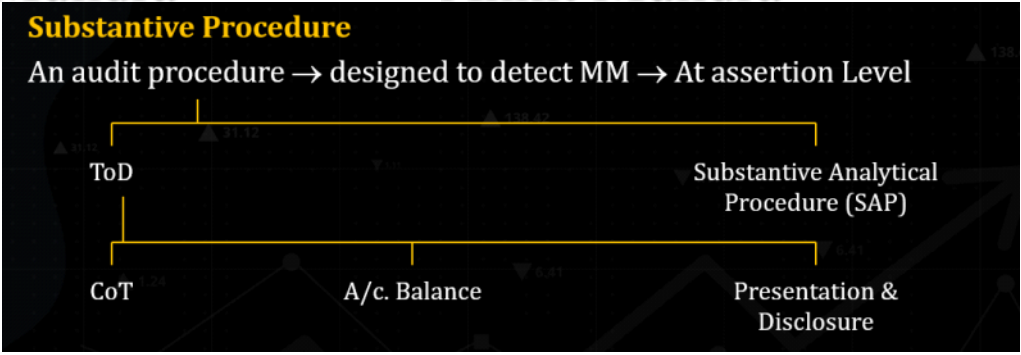
1.7a - Risk assessment procedures:

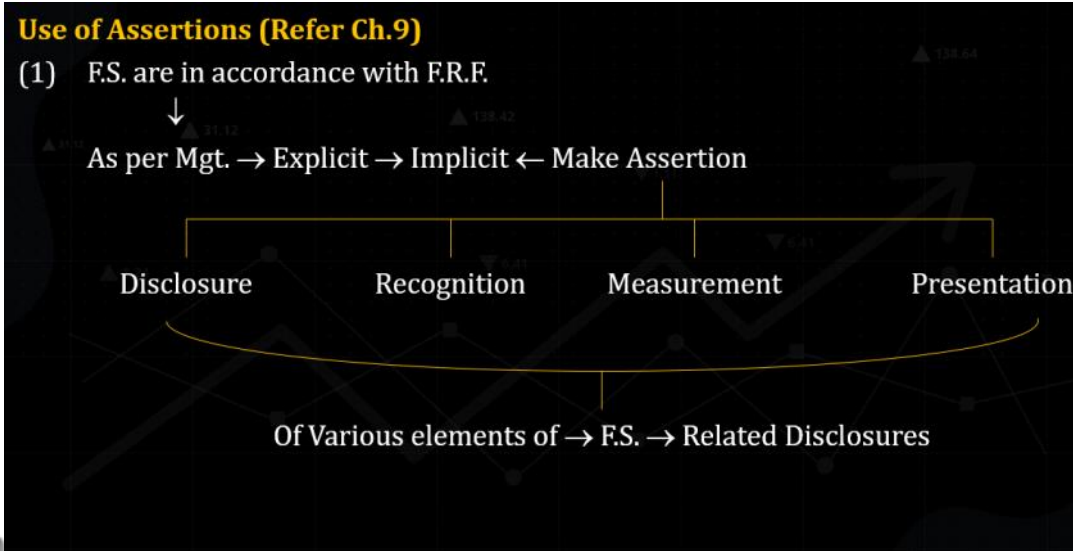
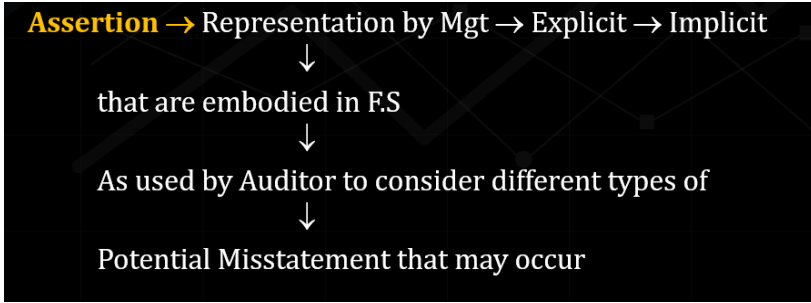


1.7.b(i) - Tests of controls



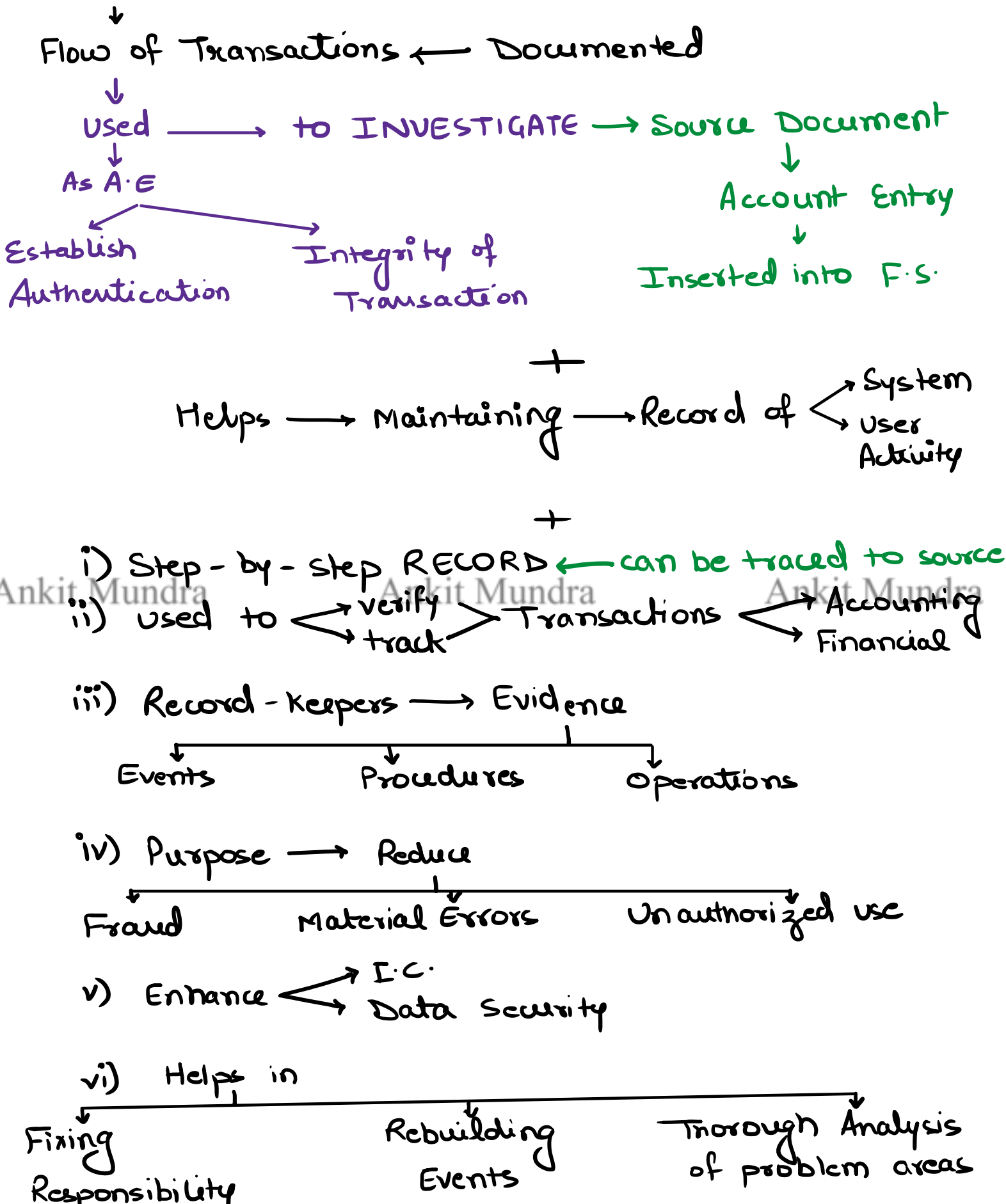
1.7.b(ii) Substantive Procedures- Tests of details and Substantive analytical procedures





→ Negative Assertions

- Express → NO Contingent Liability
- Implied → NO mention in F.S.

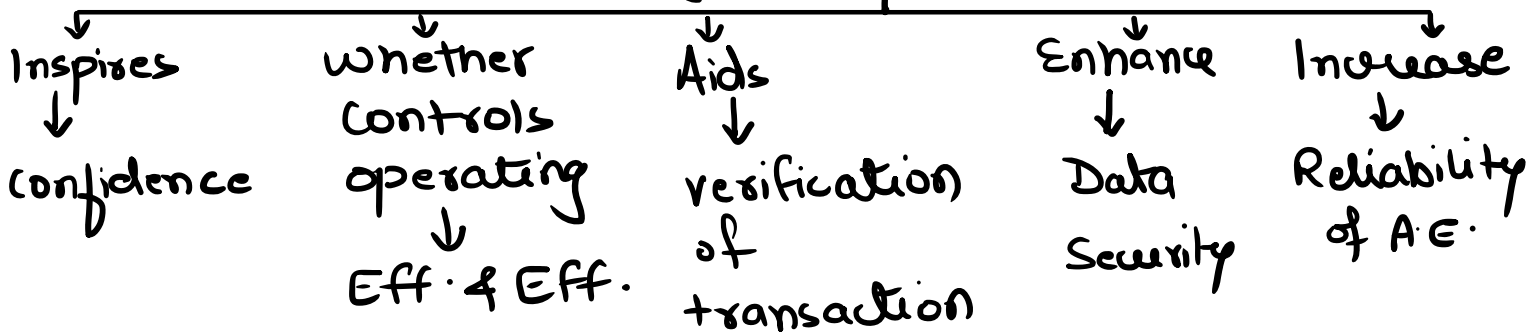


vii) Involves → COST

System expenditure  
Time for analysing data

'Automated Tools' can reduce this demerit

viii) Systems → having Audit Trails



1.10 - Information to Be Used as Audit Evidence

1.10.1 - When information to be used as audit evidence has been prepared using the work of a management's expert, the NET of audit procedures may be affected by such matters;

i) Nature complexity > Matter

ii) ROMM

iii) Alternative source → A.E → Available ?

iv) Nature  
Scope  
Objective → Mgt's Expert's Work

v) Mgt's Expert → Employed → by Entity  
→ Service Provider

vi) Extent → Mgt → Exercise control  
→ Influence → Expert's Work

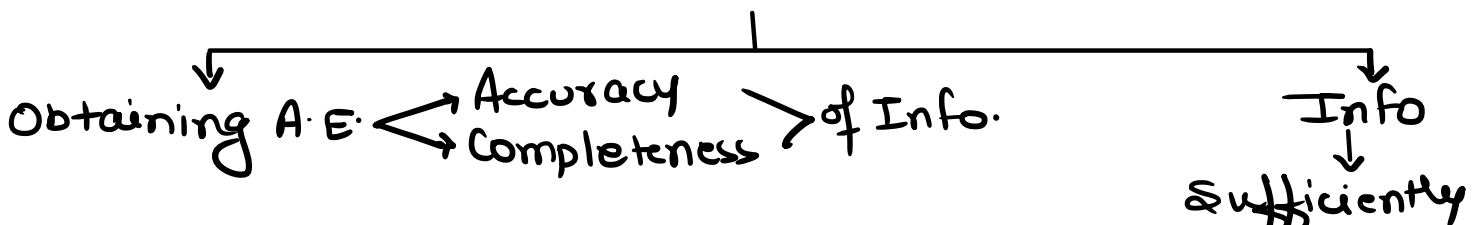
vii) Expert → subject to → Technical → Standards  
→ Professional → Requirements  
→ Industry

viii) Nature > Entity's I.C. ← OVER Expert's work  
Extent

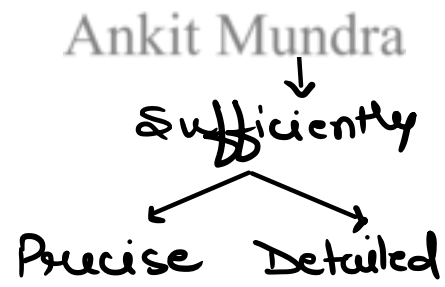
ix) Auditor's → Knowledge > Expert's field of work  
→ Experience

x) Auditor's → previous experience → Expert's work

1.10.2 - When using information produced by the entity, the auditor shall evaluate whether the information is sufficiently reliable for the auditor's purposes, including as necessary in the circumstances:



Ankit Mundra ... → Completeness T



Ankit Mundra

Ankit Mundra

Ankit Mundra

Ankit Mundra

Ankit Mundra

Ankit Mundra

When designing  $\begin{cases} \rightarrow \text{ToC} \\ \rightarrow \text{ToD} \end{cases} > \text{Auditor shall determine}$

**MEANS OF SELECTING ITEMS FOR TESTING**

Based on Auditor's Judgment

Selecting ALL Items  
(100% Examination)

Selecting Specific Items

Audit Sampling  
↓  
Discussed Later

Auditor MAY decide

Factors

Most Appxo.

Examine

Auditor's understanding of Entity

Assessed ROMM

Characteristic of Population

Entire Population

CoT

A/c Bal.

Stratum

NON SAMPLING RISK

Examples

100% Examination

→ Unlikely → ToC

→ Appxo. → ToD

- ① High VALUE items
- ② > certain amounts
- ③ To obtain info.

Population

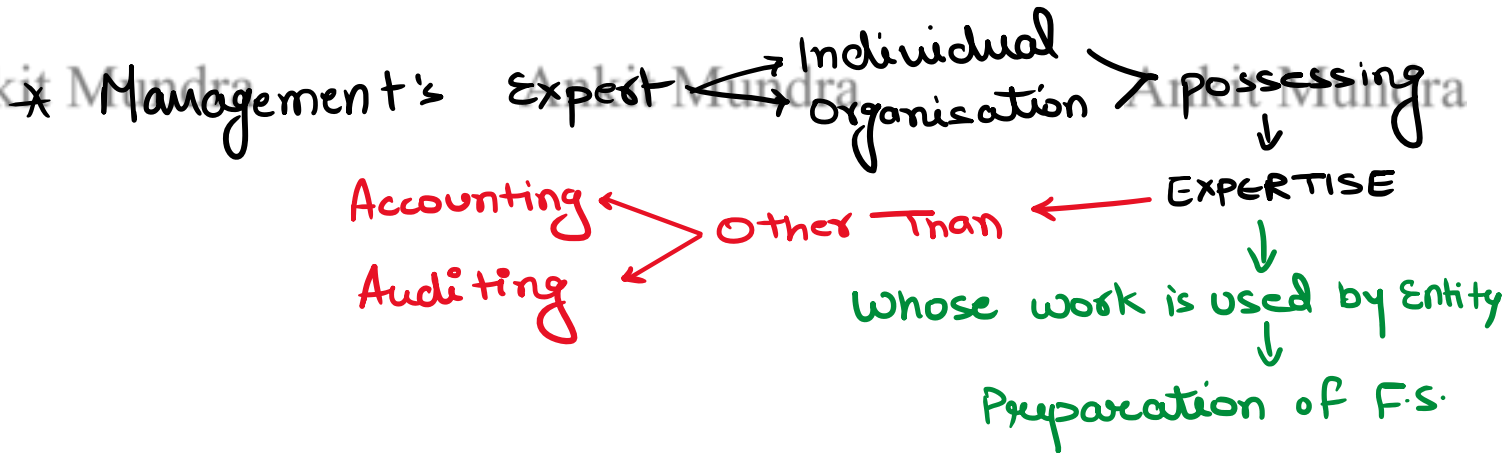
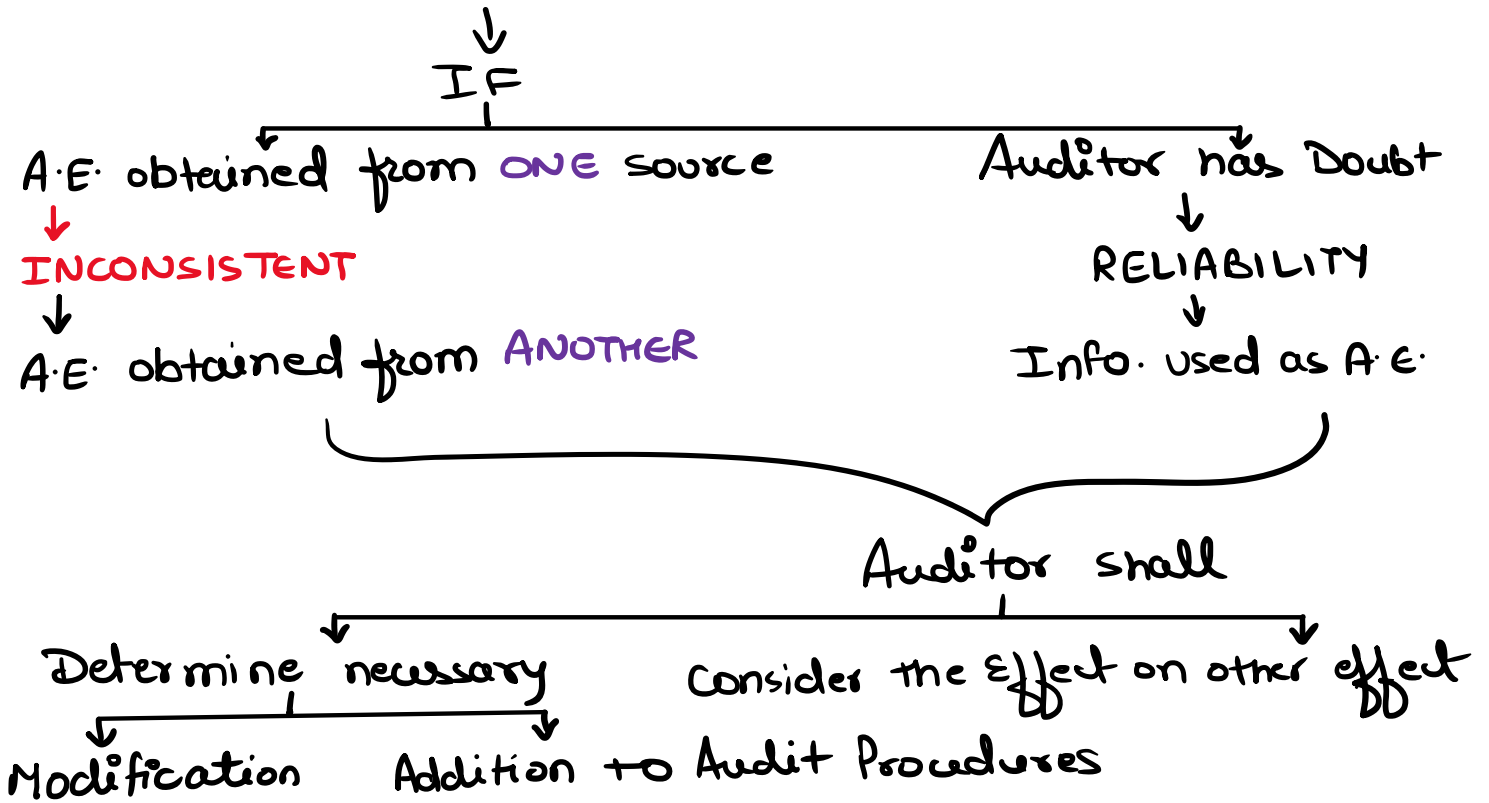
Large VALUE Items

Significant RISK

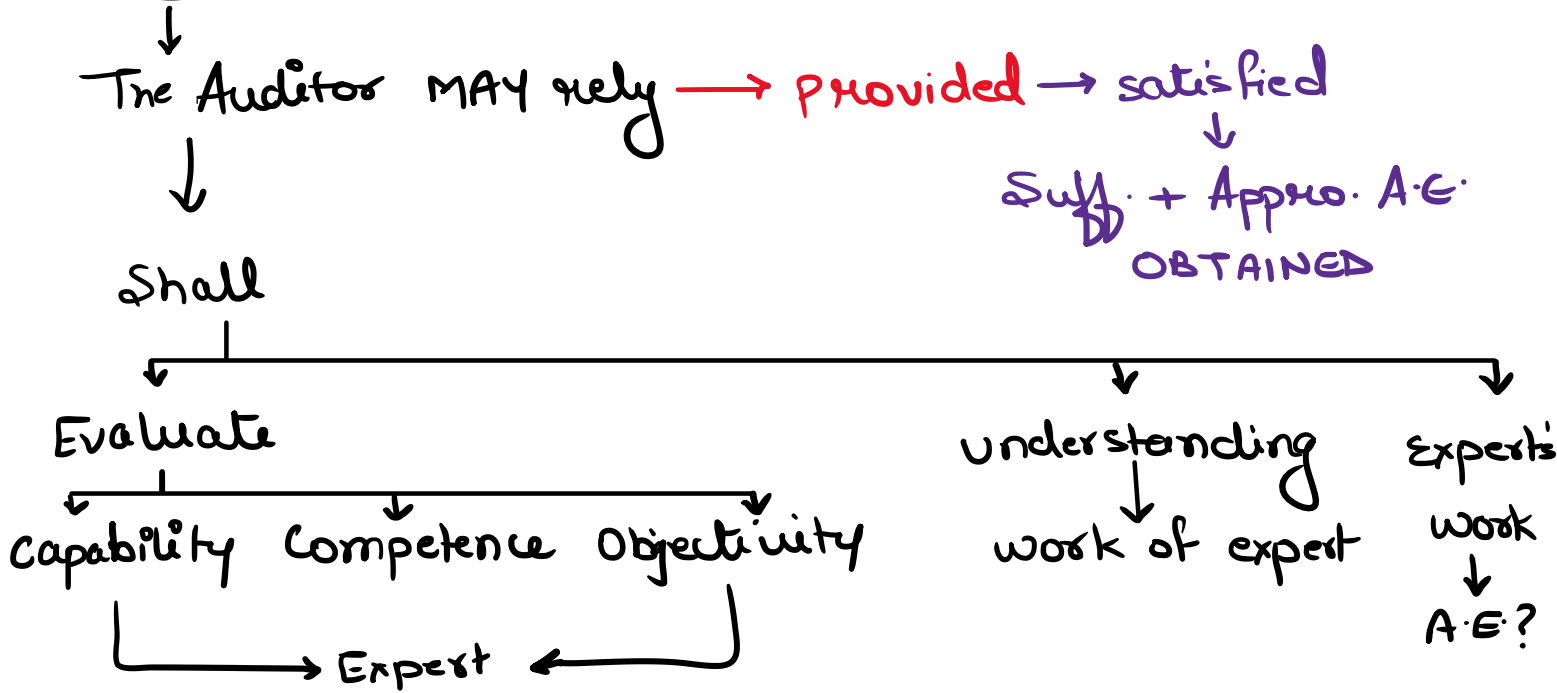
Process

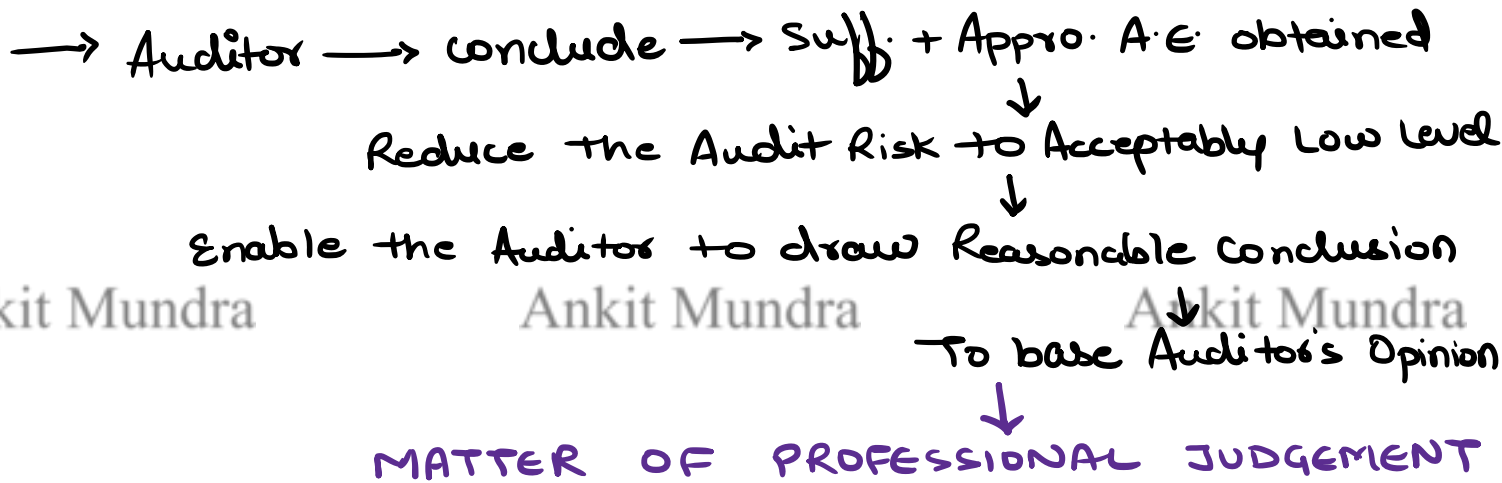
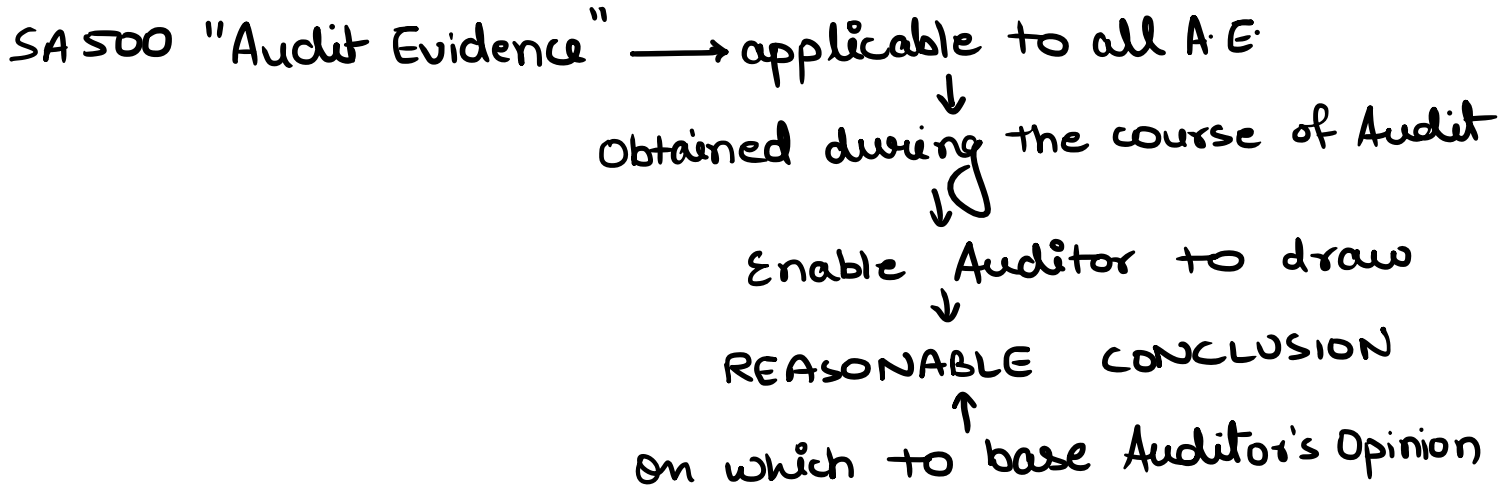
REPETITIVE AUTOMATIC

1.12 - Inconsistency in or Doubts over Reliability of Audit Evidence

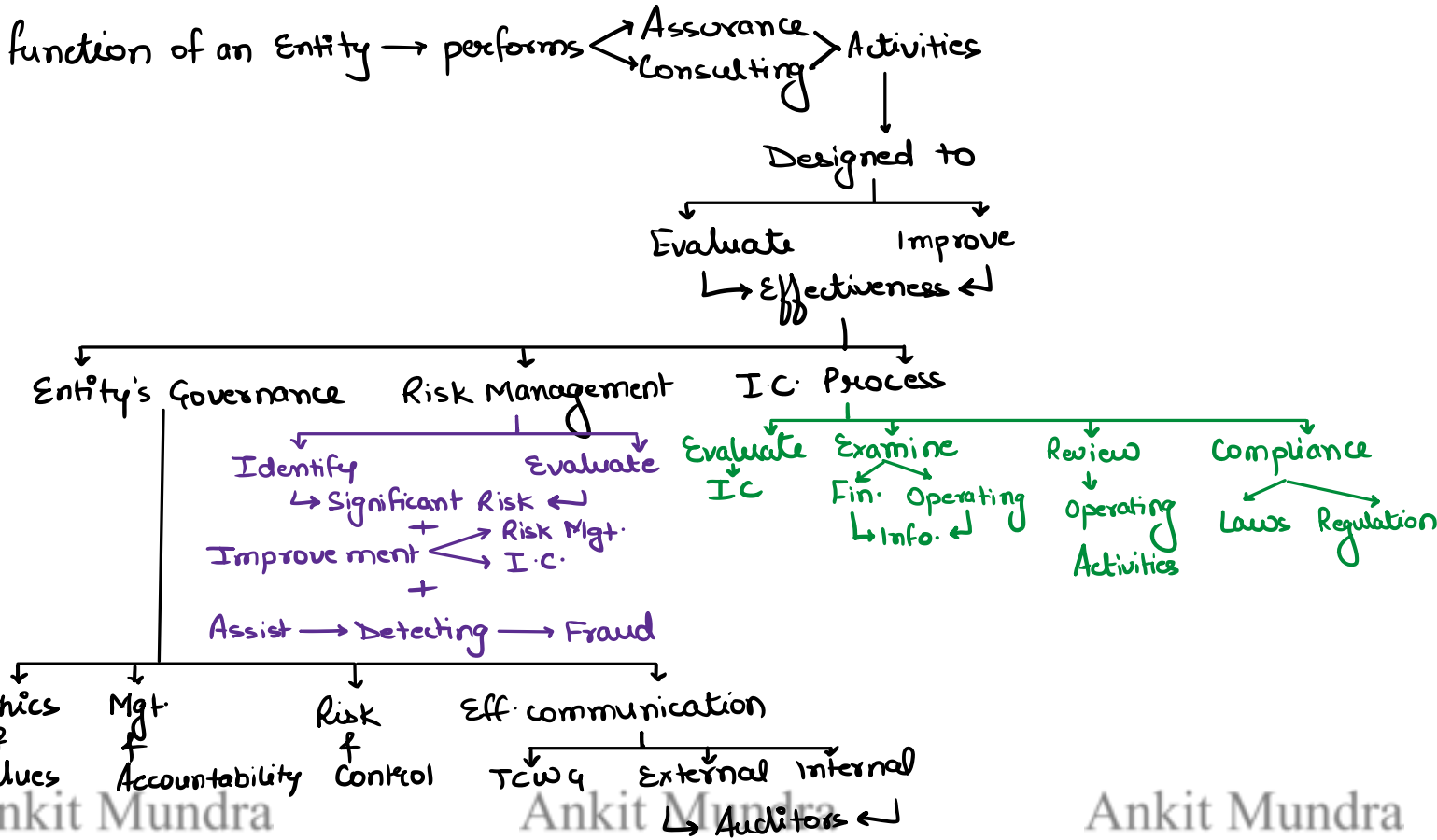


1.13 Relying on the work of a management's expert

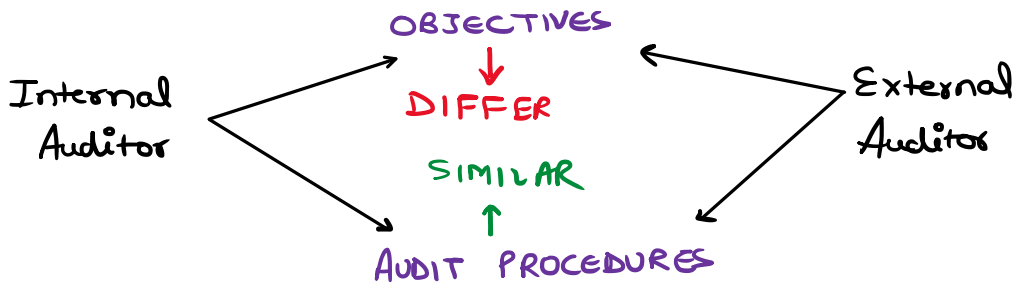




2.1 - Definition of Internal Audit Function

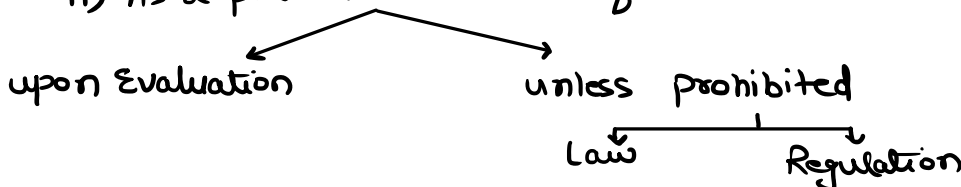


2.2 - Ways in which the external auditor may make use of the function for purposes of the audit.



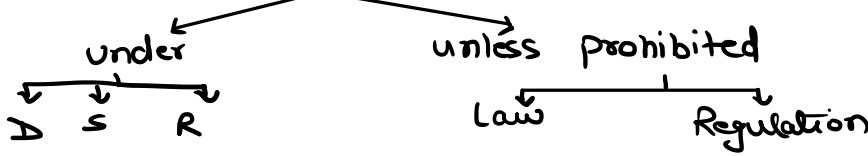
→ External Auditor → MAY make use of function:

- i) To obtain Info → Relevant for assessing ROMM
- ii) As a partial substitution for A.E. to be obtained

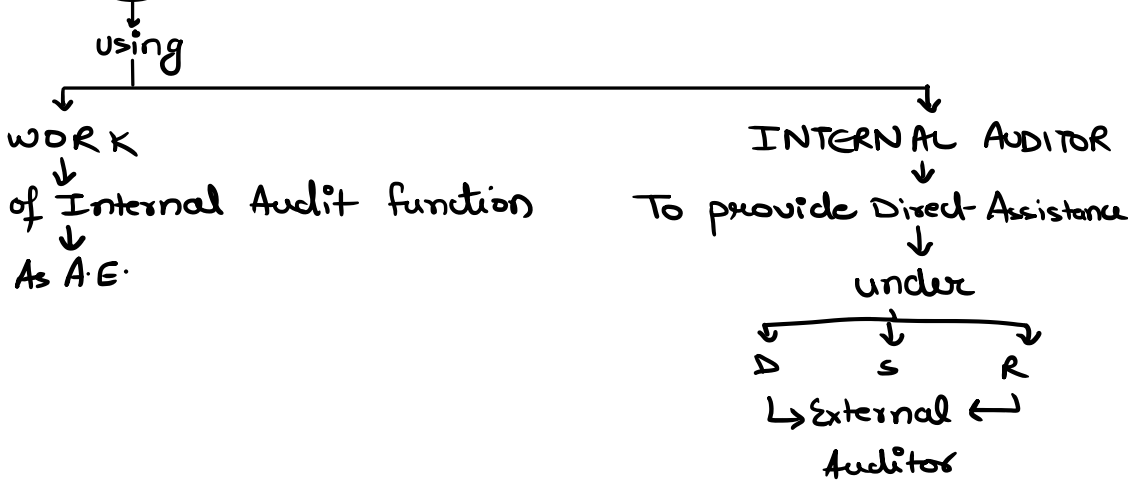


iii) Use 'Direct Assistance' → from Internal Auditors

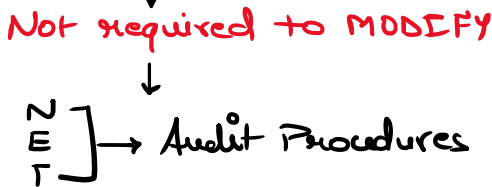
iii) Use 'Direct Assistance' → from Internal Auditors



2.3 (Scope of SA 610)

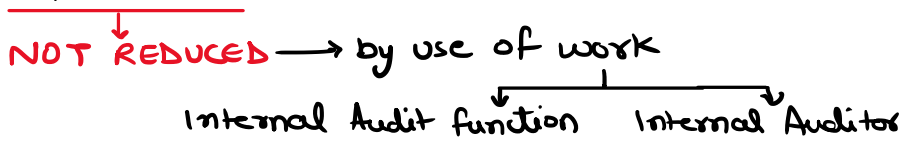


→ External Auditor



2.4 - External Auditor's Responsibility for the audit

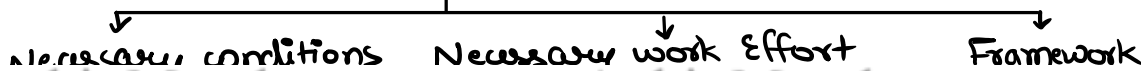
i) Sole Responsibility → External Auditor

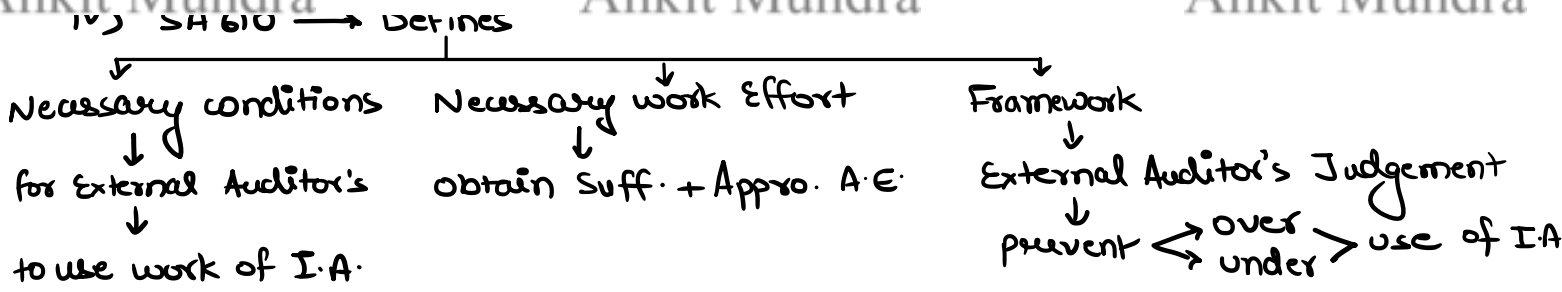


ii) May perform → similar → Audit Procedures

iii) Internal Audit Function  
 Internal Auditor } NOT INDEPENDENT  
 ↓  
 As per SA 200

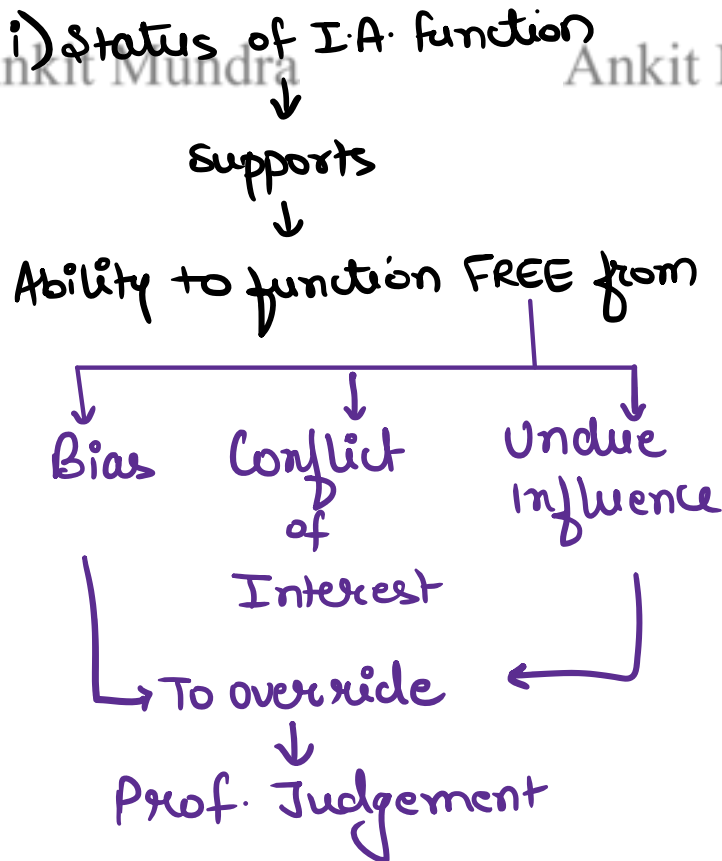
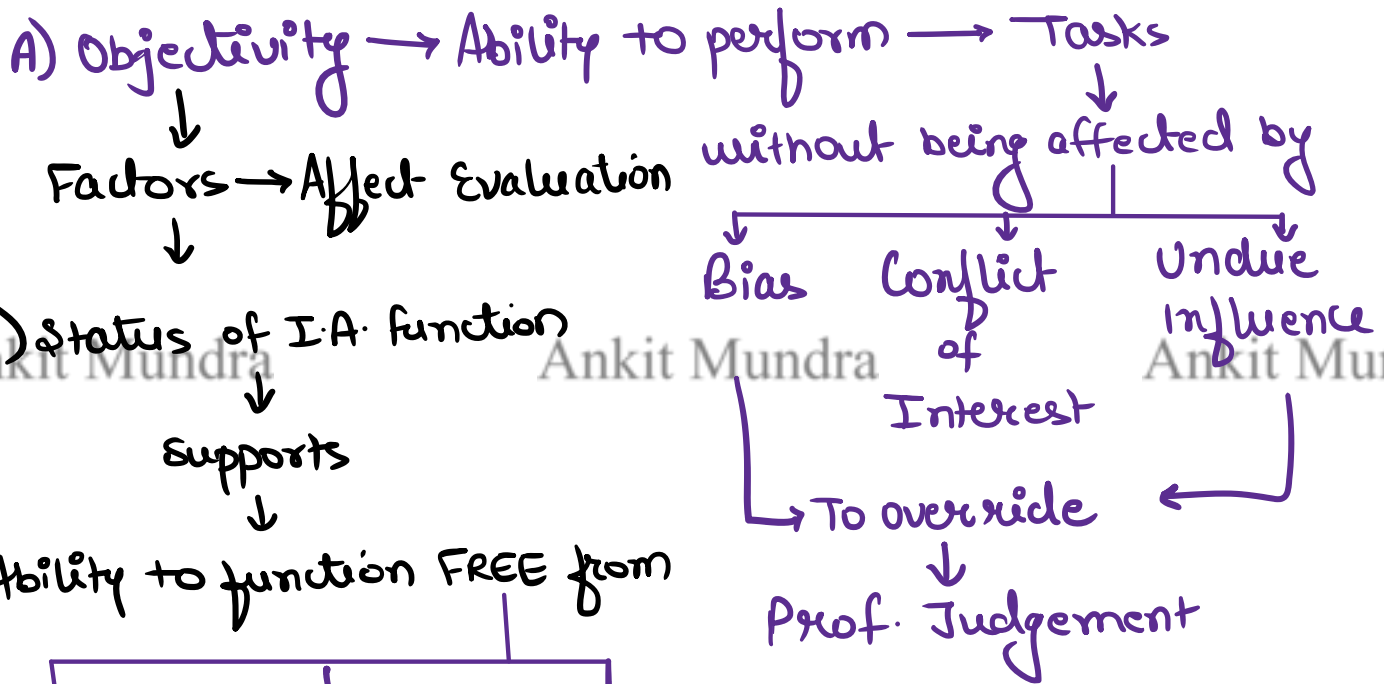
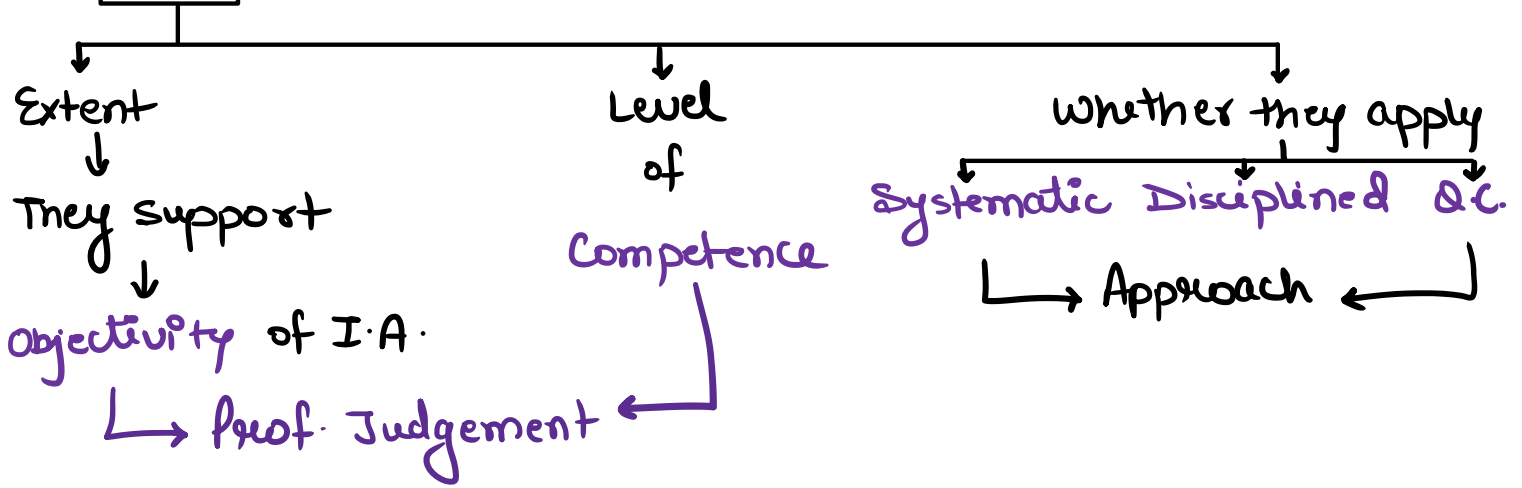
iv) SA 610 → Defines







2.6 - Evaluating the Internal Audit Function



ii) TCWG → oversee → Employment Decisions

iii) Constraints  
Restrictions } By  $\begin{cases} \text{Mgt.} \\ \text{TCWG} \end{cases}$  } on  $\rightarrow$  I.A. Functions

iv) I.A. Functions  $\rightarrow$  Free From  $\rightarrow$  Conflicting Responsibility

b) Competence  $\begin{cases} \text{Attainment} \\ \text{Maintenance} \end{cases}$  } Knowledge + skills

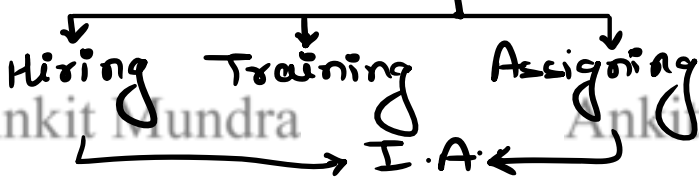
Factors  $\rightarrow$  Affect Evaluation

At a level to enable

i) I.A.F.  $\begin{cases} \text{Adequately} \\ \text{Appro.} \end{cases}$  } Resourced

Assigned tasks performed  
 $\begin{cases} \text{Diligently} \\ \text{Prof. Standards} \end{cases}$

ii) Established policies for



I.A. Assignments

Technical

iii) I.A.  $\rightarrow$  Adequate  $\begin{cases} \text{Training} \\ \text{proficiency} \end{cases}$  } in Auditing

iv) I.A.  $\rightarrow$  possess  $\rightarrow$  Knowledge relating to  $\rightarrow$  Entity's  
 $\begin{cases} \text{F.R.} \\ \text{F.R.F.} \end{cases}$

Objectivity and competence may be viewed as a continuum  $\rightarrow$  continuous series

More  $\rightarrow$  I.A. function's  $\begin{cases} \text{Organisational Status} \\ \text{Relevant P\&P} \end{cases}$  } Adequately  
 Support Objectivity



Higher the level of Competence

More likely E.A. use I.A.F.

Objectivity: CANNOT compensate for lack of Suff. Competence of I.A.F.

Competence: CANNOT compensate for Org. status  
P&P } That do not support OBJECTIVITY of I.A.

c) Systematic & Disciplined Approach → To



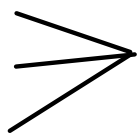
Distinguishes the Activities of I.A.F.

from other Monitoring Control Activities

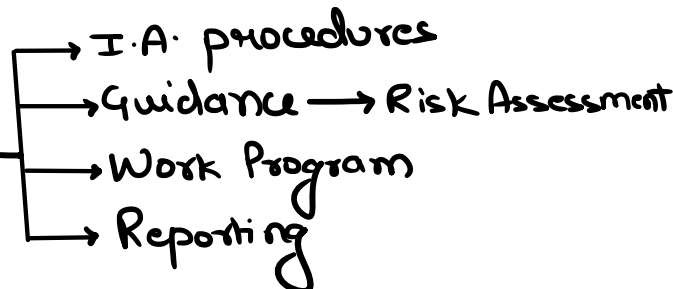
Factors → Affect Evaluation



i) Existence  
Adequacy  
Use

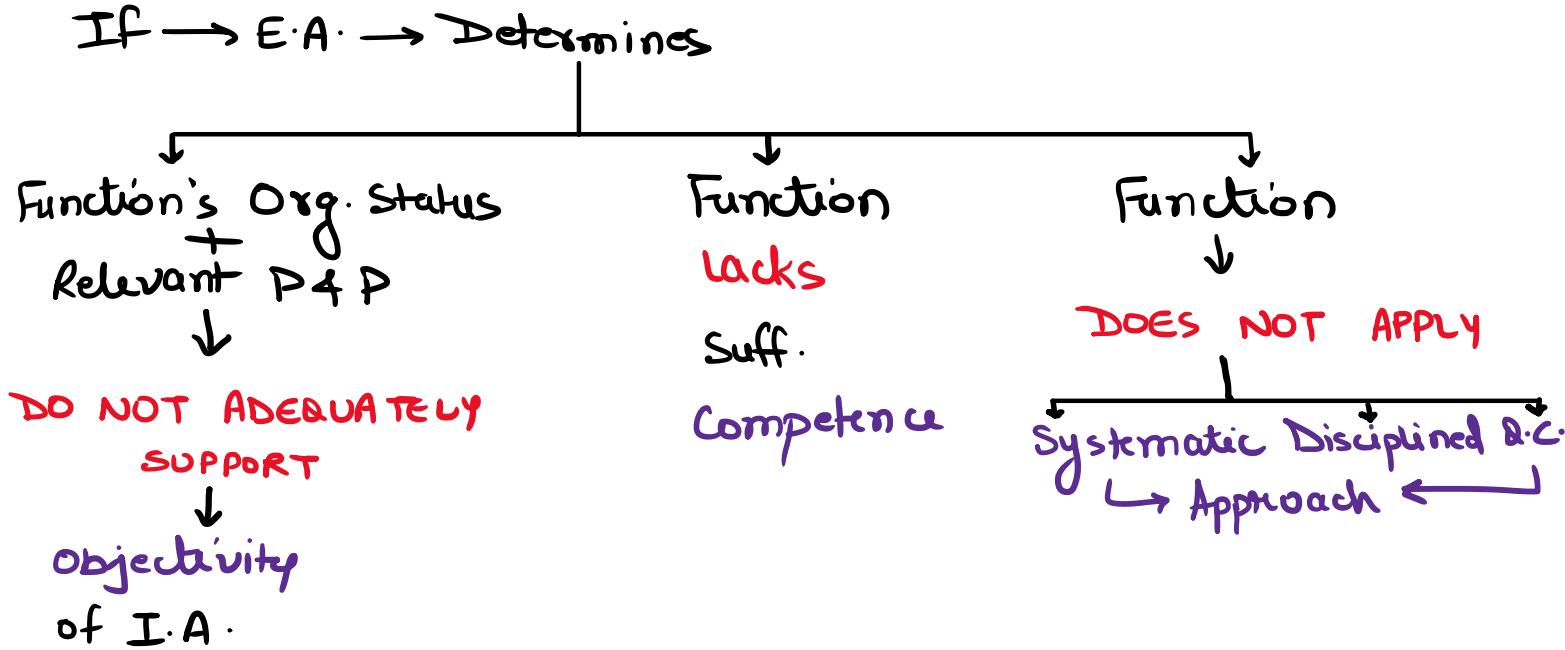


Documented



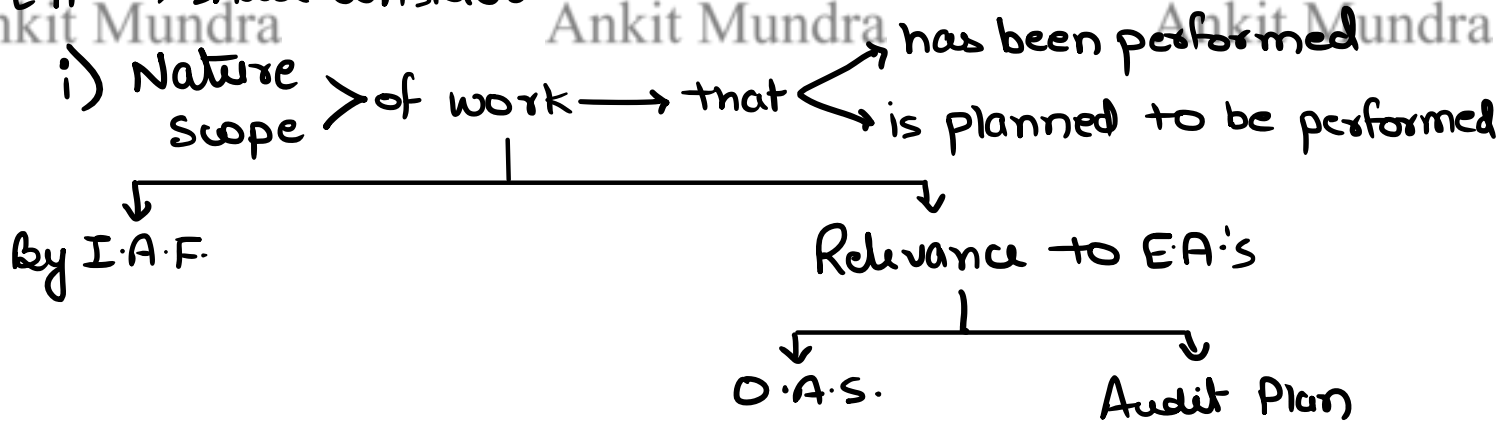
ii) I.A.F. → Appxo. → D.C. → P P P

2.7 - Circumstances When Work of the Internal Audit Function Cannot Be Used



2.8 - Determining the Nature and Extent of Work of the Internal Audit Function that Can Be Used

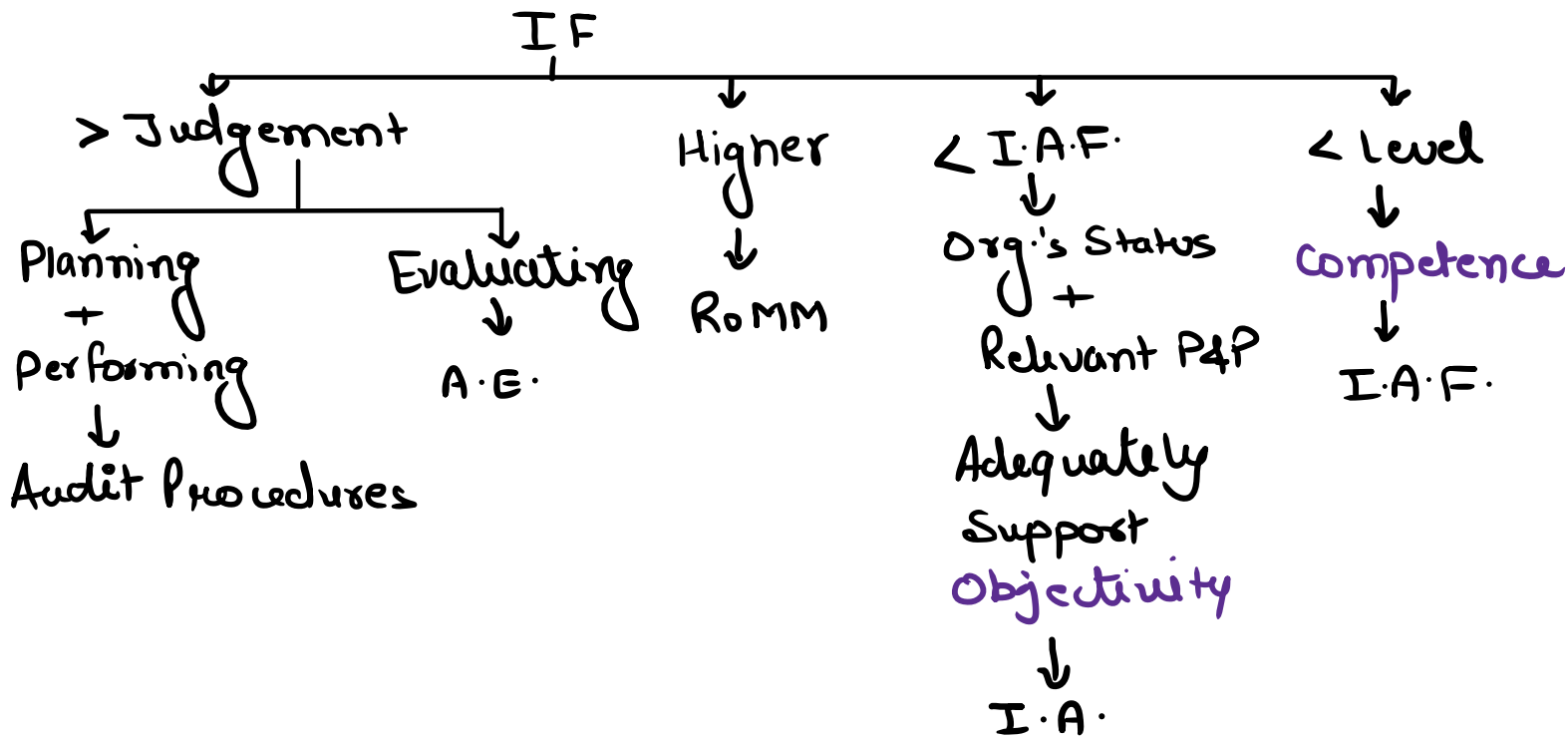
E.A. → shall consider :



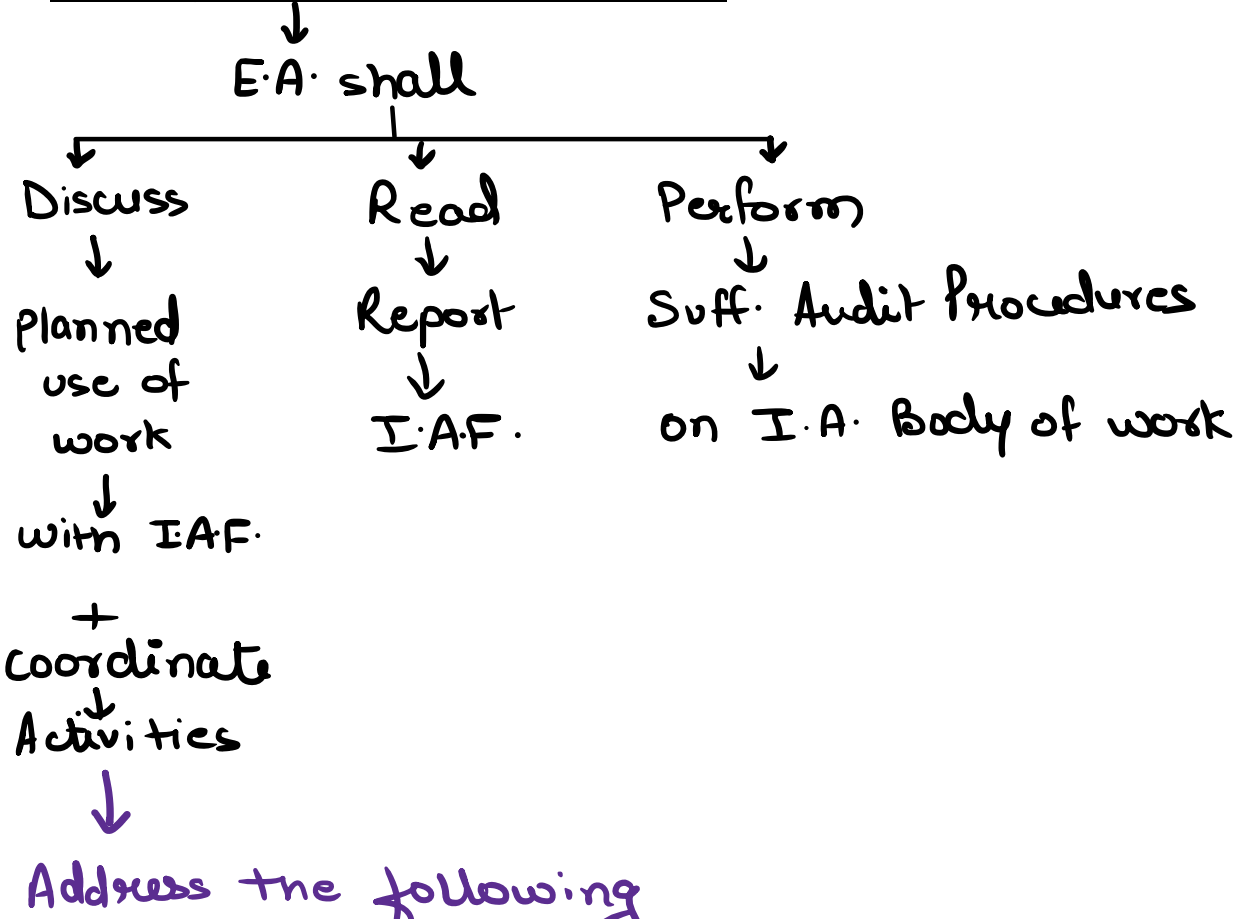
\* Examples

ToC  
 Substantive Procedures  
 Observation → Inventory Count  
 Tracing → I.S.  
 Testing → Compliance → Legal Regulatory Req.

2.9 - Circumstances in which the external auditor shall plan to use less of the work of the Internal audit function and perform more of the work directly



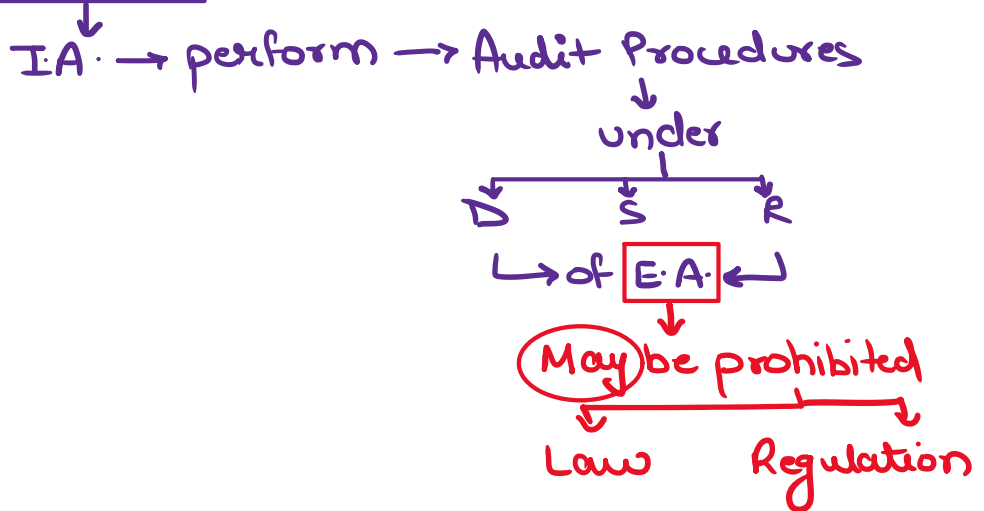
2.10 - Using the Work of the Internal Audit Function



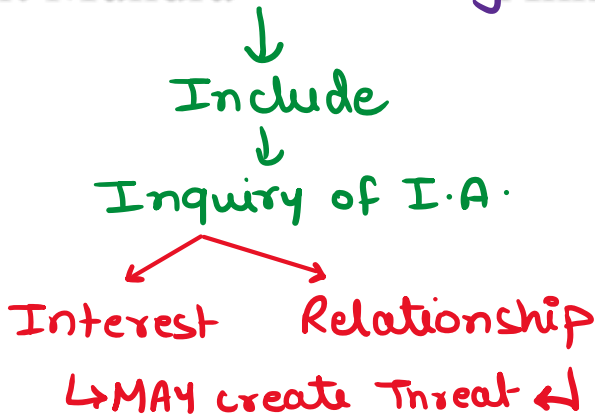
Address the following

- i) N
  - ii) E
  - iii) T
- of Audit work
- iv) DM + PM
  - v) Methods of Item Selection + Sample Size
  - vi) Documentation
  - vii) Review > Reporting Procedures

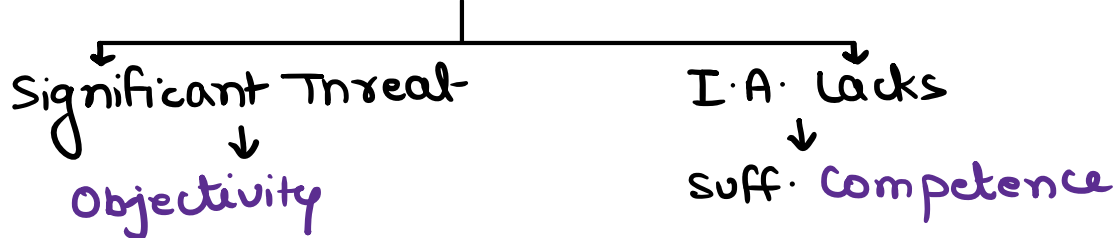
2.11 Determining **Whether**, in **Which Areas**, and to **What Extent** Internal Auditors Can Be Used to Provide Direct Assistance



IF NOT PROHIBITED → E.A. shall → Evaluate

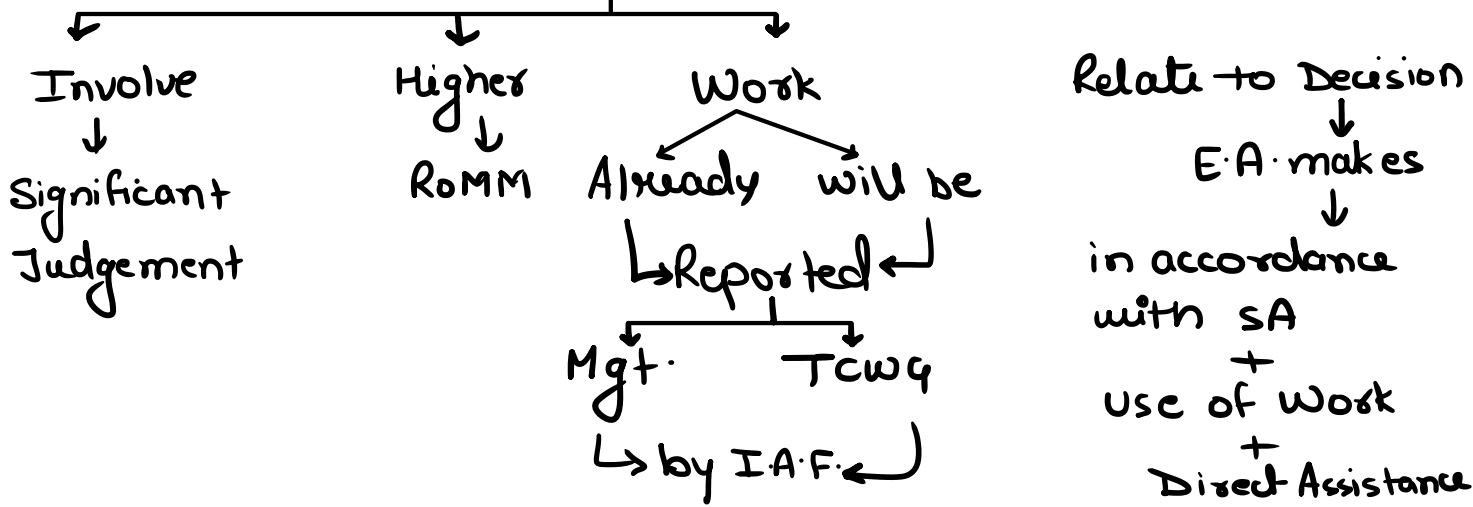


The external auditor shall not use an internal auditor to provide direct assistance if:



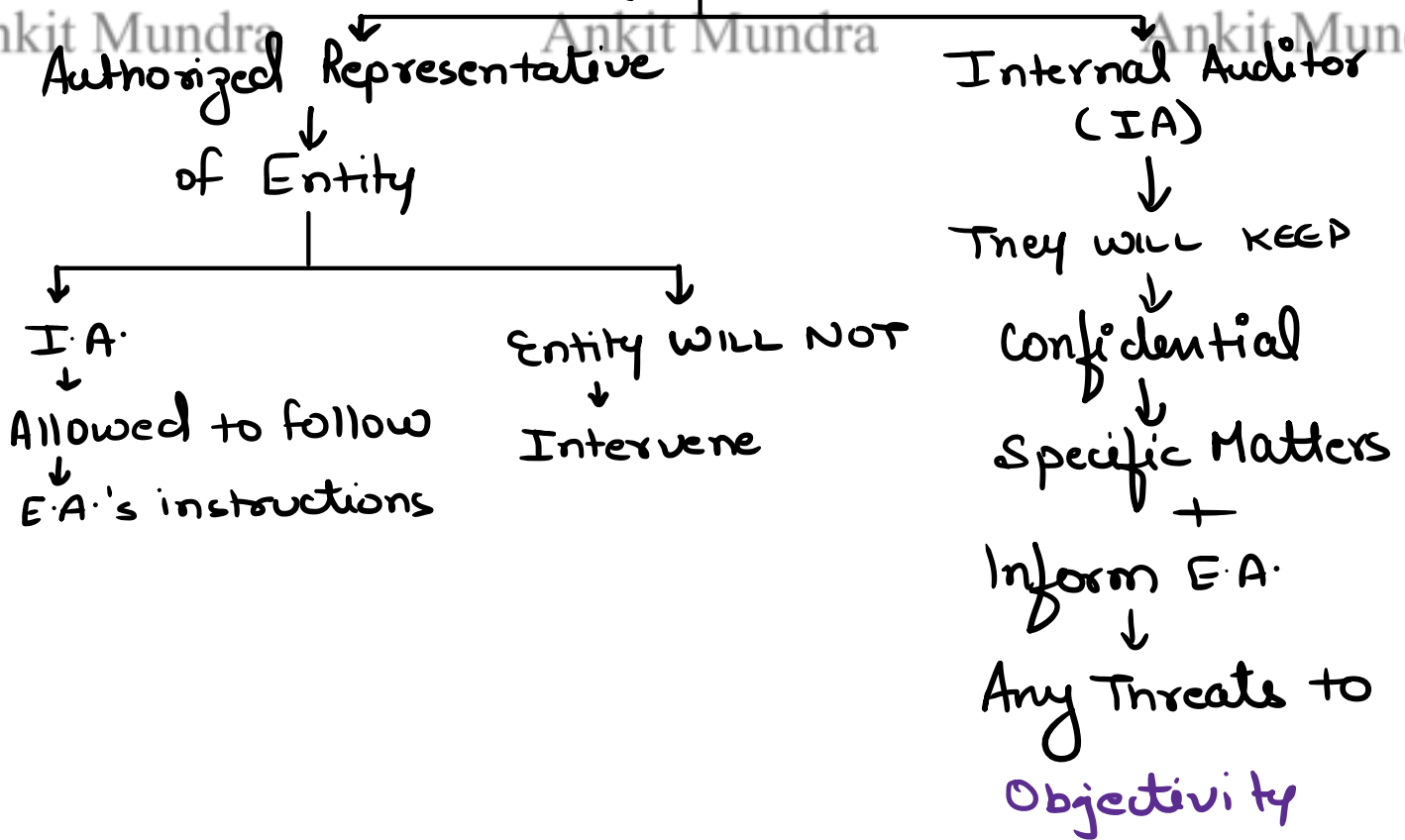
The external auditor shall not use internal auditors to provide direct assistance to perform procedures

The external auditor shall not use internal auditors to provide direct assistance to perform procedures that:



Prior to using internal auditors to provide direct assistance for purposes of the audit, the external auditor shall:

Obtain → Written Agreement



(Already discussed in Ch. 3)

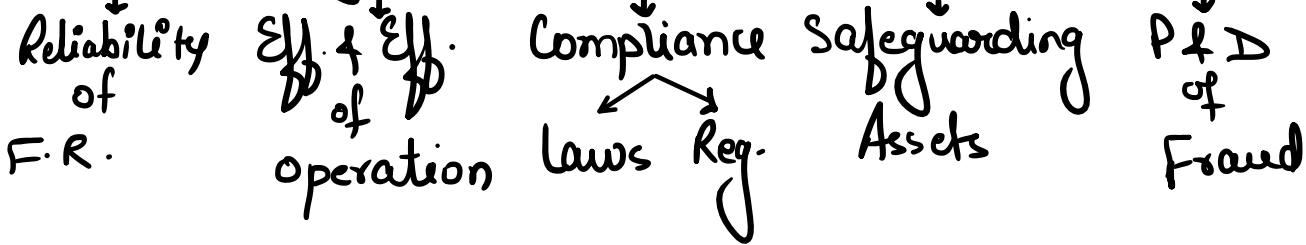
<u>Internal Financial Control</u> Wider Term	Distinction b/w	<u>Internal Control over financial reporting</u> Narrower Term
---	-----------------	---

↓  
P & P ← By Companies

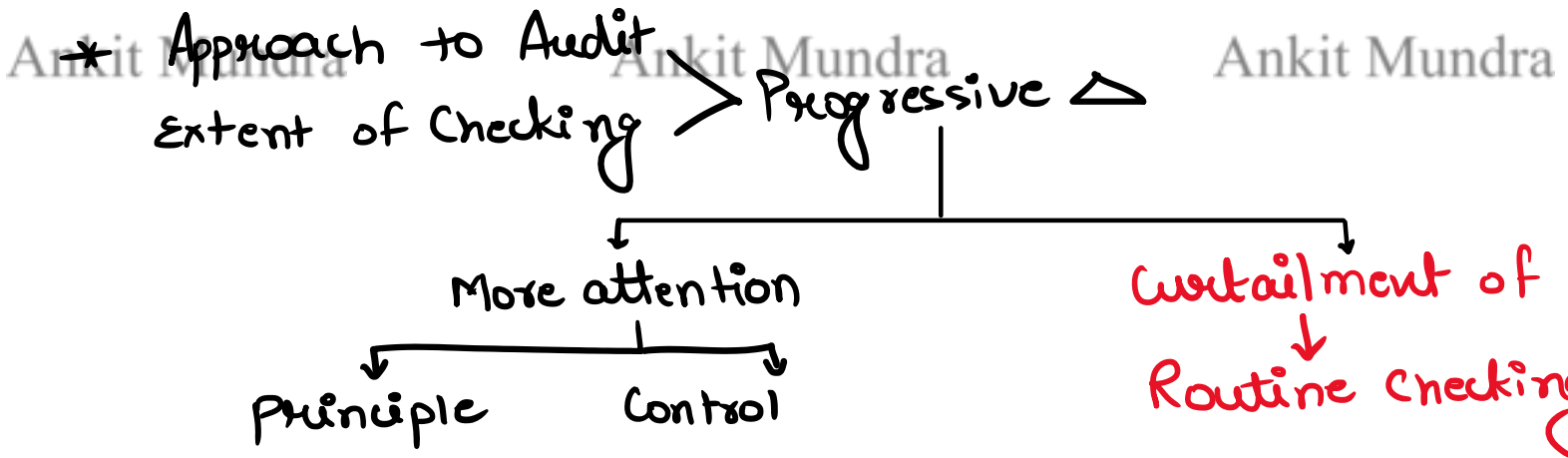
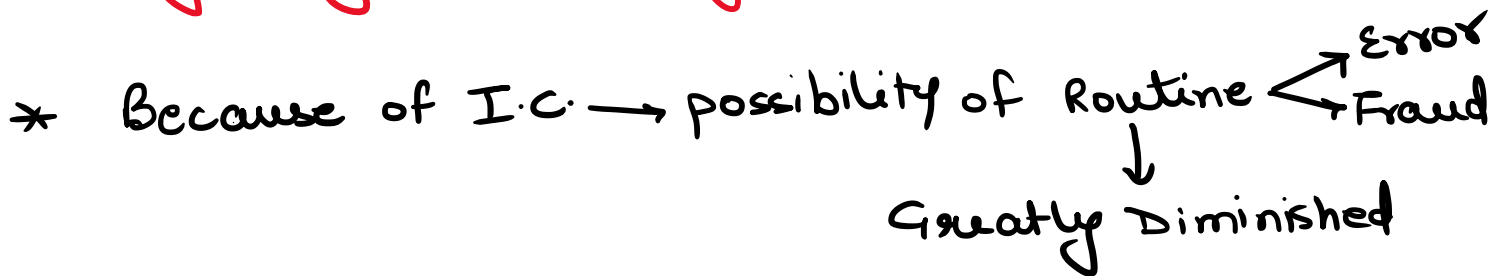
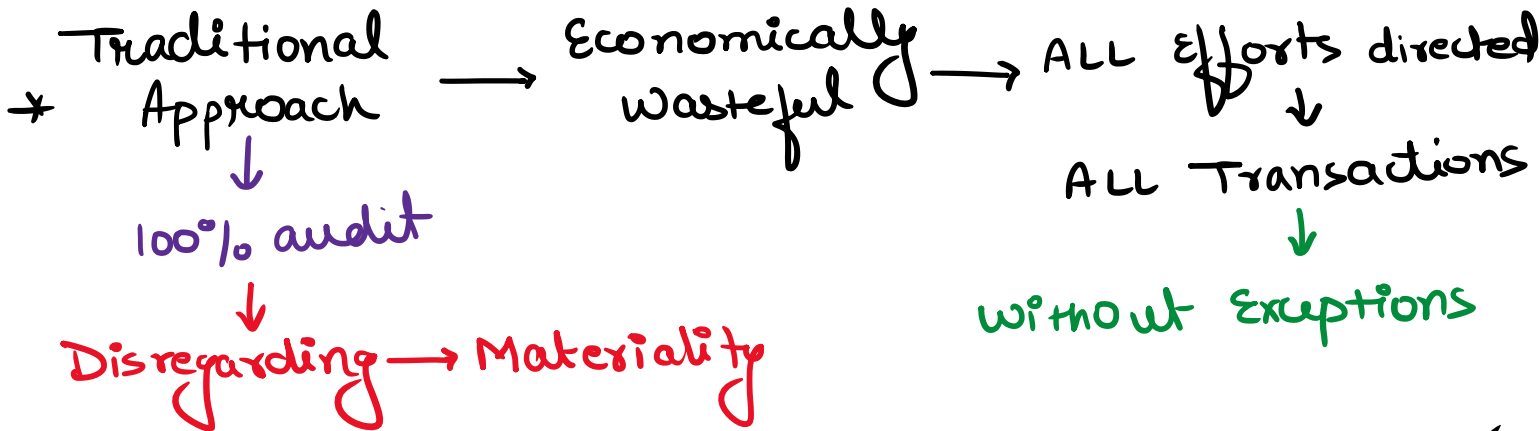
↓  
Auditor's are REQUIRED  
To Express an opinion on it

↓  
Ensuring

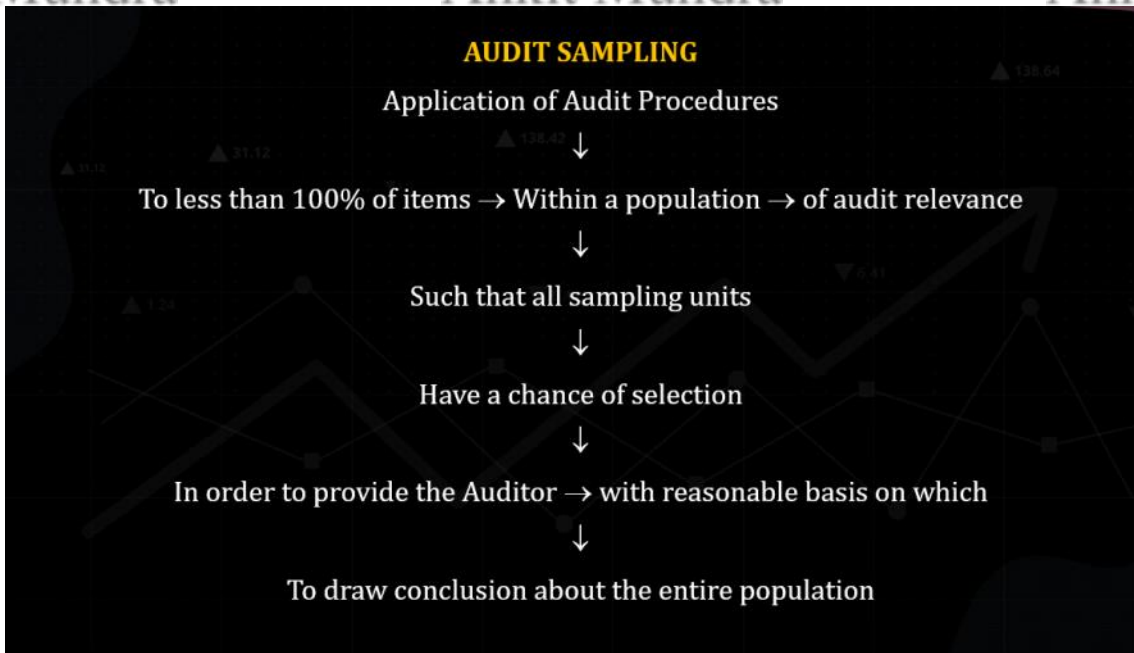
Additional Distinct

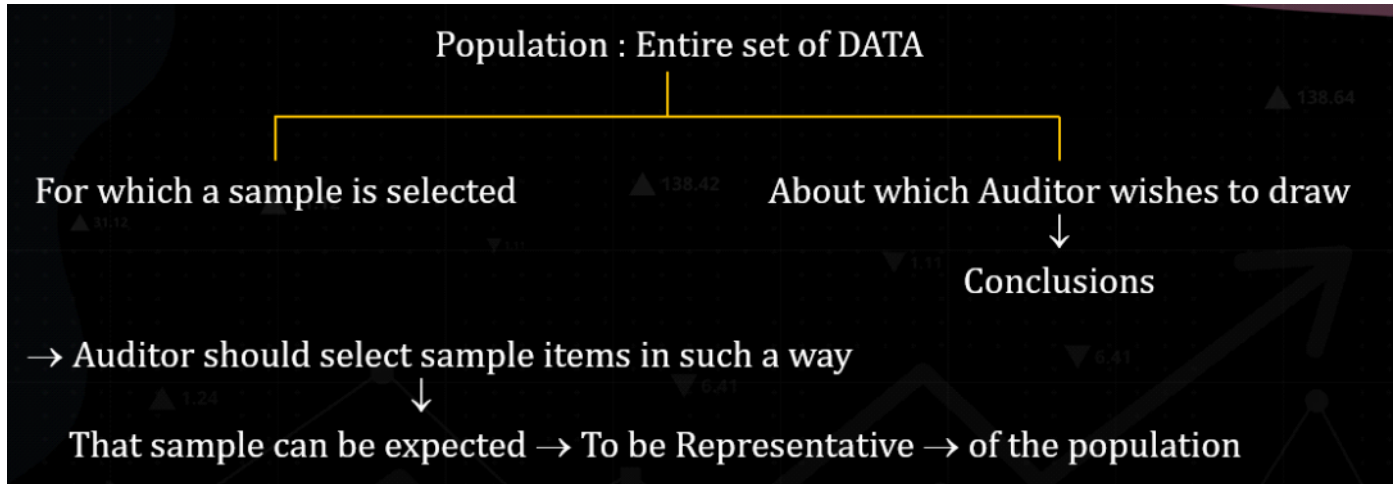


3.1 - Sampling: An Audit Procedure

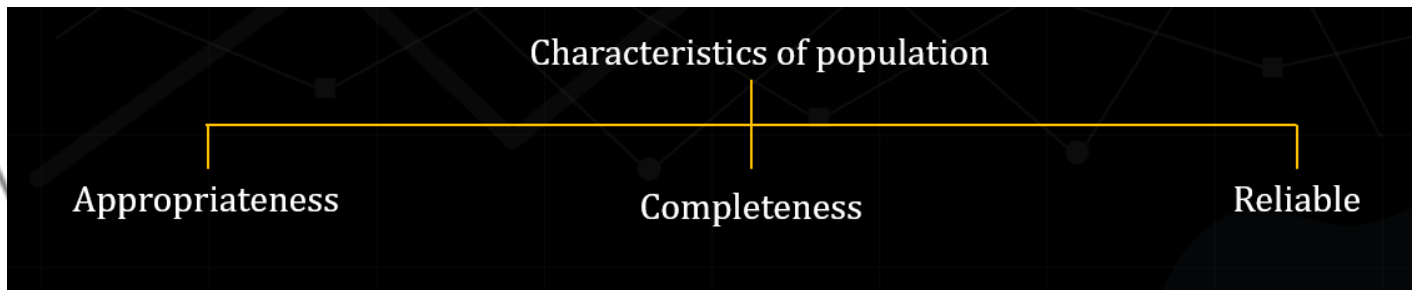


3.2 Meaning of Audit Sampling





### 3.3.1 - Characteristics of Population



3.4 - Sampling Unit

Individual Items → that make up the population

Audit Procedure are applied → conclusion drawn from them

Projected on the POPULATION

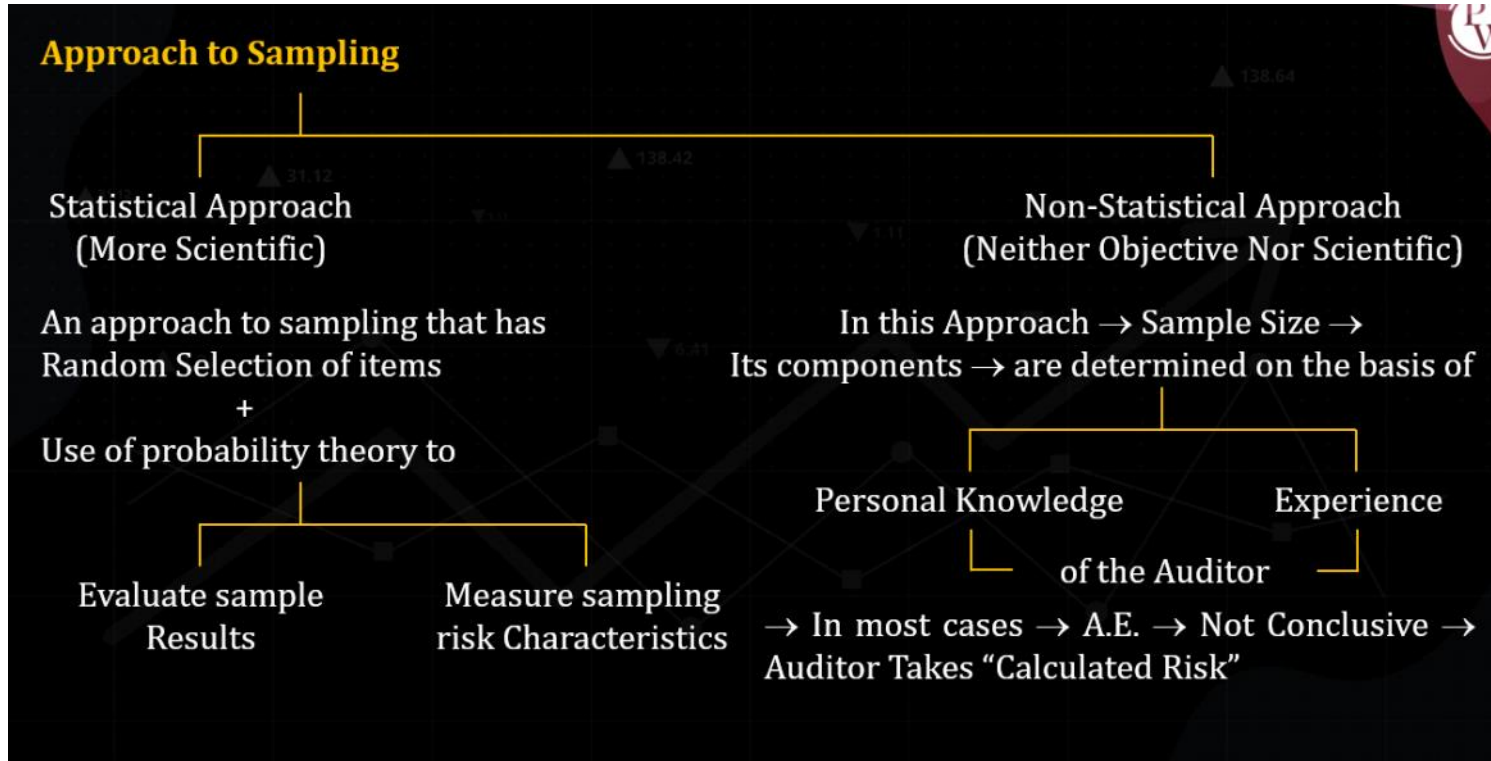
→ Sample must be REPRESENTATIVE → Closely similar  
→ Not exactly same

Statistical

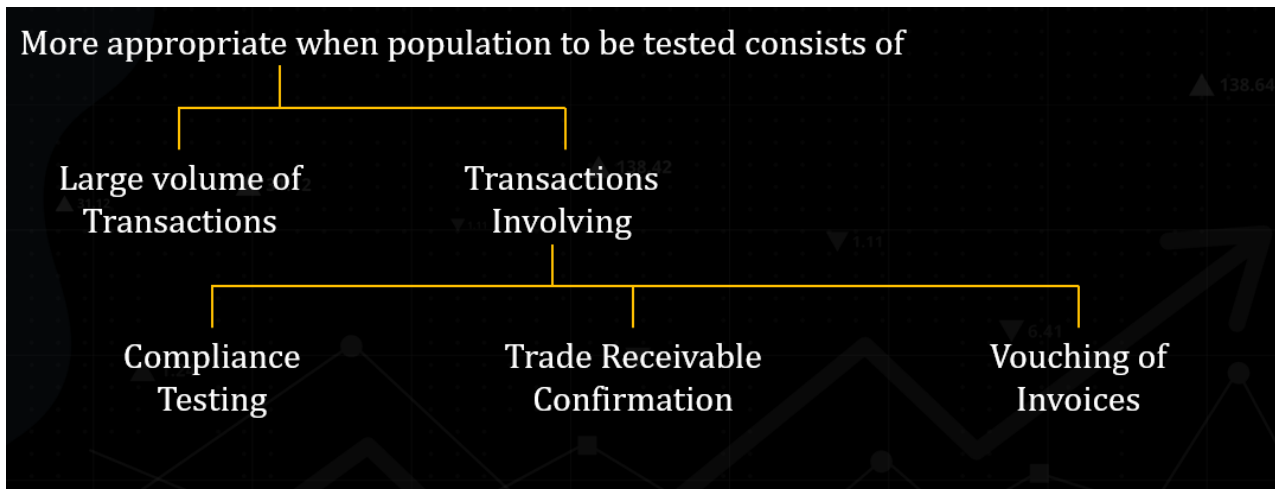
Non-Statistical

Approach

3.5 Approaches to Sampling (Types of Sampling)



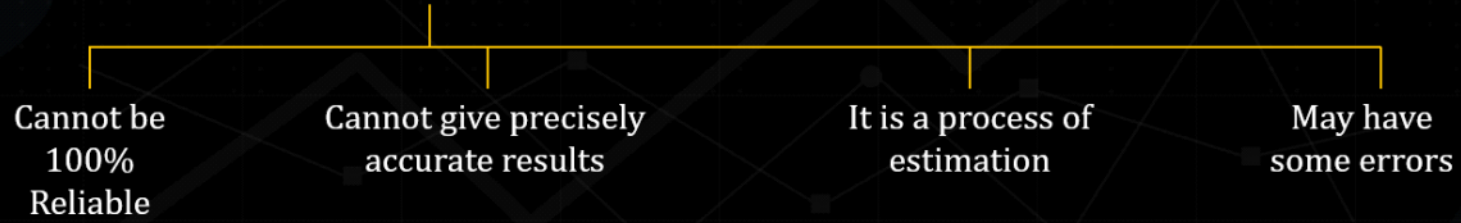
3.5A - Statistical Sampling-More Scientific



3.6 Sampling Vs Traditional method of Auditing

**Factors to be considered**

- (1) Size of the organization under Audit
- (2) State of I.C.
- (3) Adequacy → Reliability → of → Books → Records
- (4) Tolerable error range
- (5) Degree of desired confidence

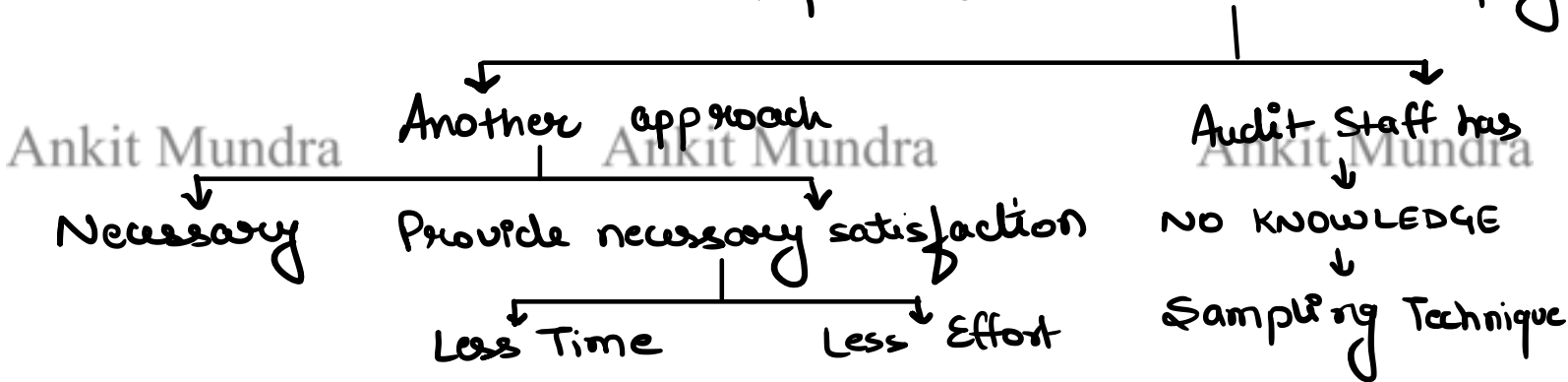


**Appropriateness of Sampling Approach**

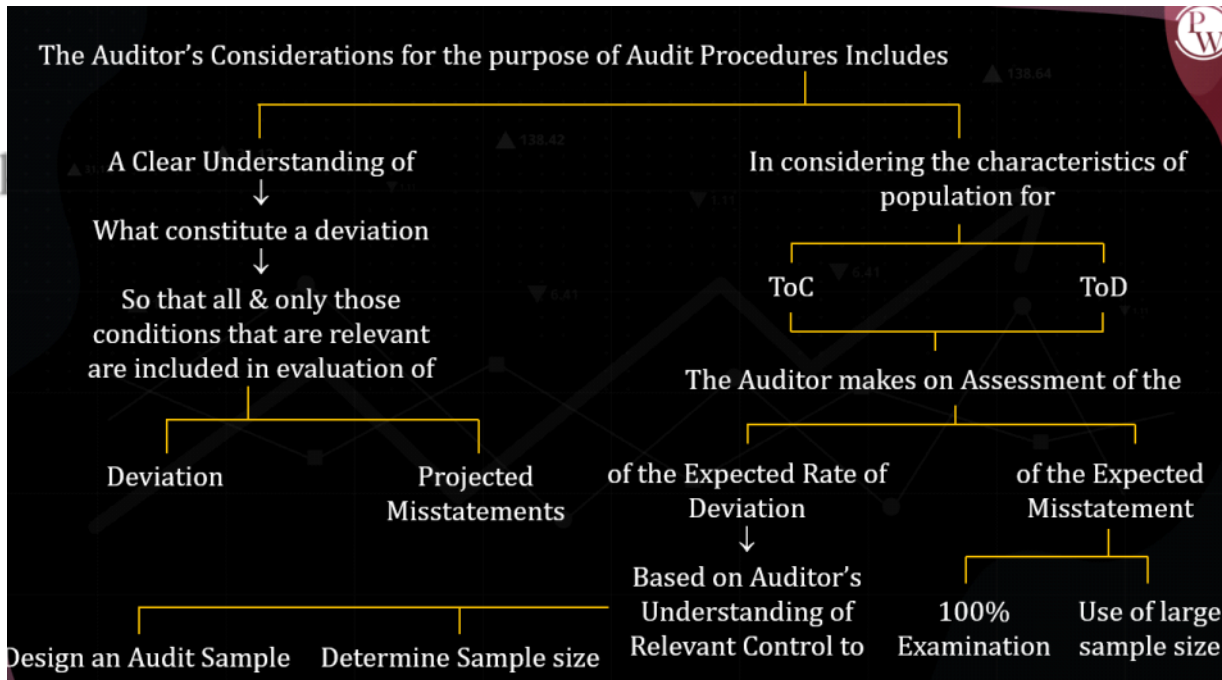
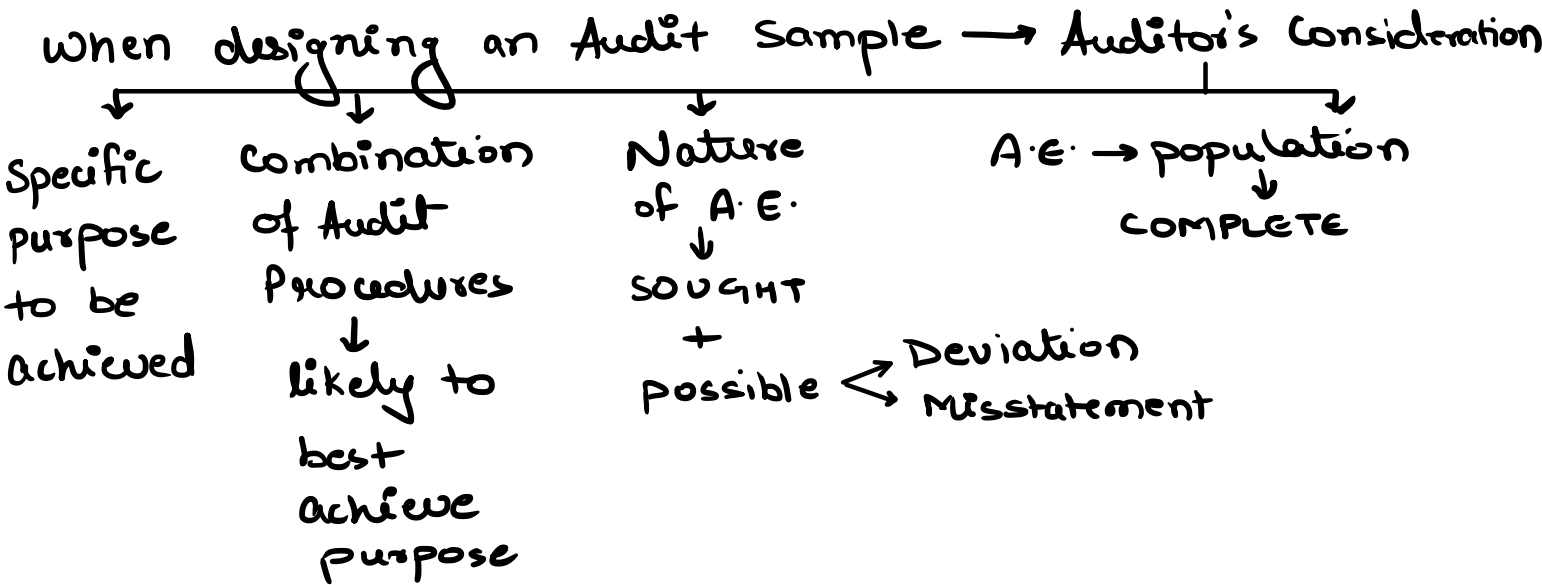
**Advantage of statistical Sampling**

- (i) The amount of testing (Sample Size) does not increase in proportion  
↓  
To the increase in size of area (universe) to be tested
- (ii) The sample selection is more objective & thereby more defensible
- (iii) The method provides a means of estimating a minimum sample size → Associated with a specific → Risk → Precision
- (iv) It provides a means of deriving a i.e. probable difference in result due to use of sample in lieu of examining All the records in the group (Universe) → Using the same Audit Procedure → Calculated Risk → Corresponding Precision(Sampling Error)
- (v) It may provide a better description of large mass of data than a complete examination of all the data, since non-sampling errors such as → Processing → Clerical Mistakes → Are not as large

Auditor should **NOT** attempt to use STATISTICAL Sampling



# \* Sample Design



## 3.9.1A - Stratification and Value-Weighted Selection

## Stratification &amp; Value Weighted Selection

SA-530 provides guidance to the Auditor on the use of :

## (A) Stratification (Division of Something into Group)

- (i) Audit efficiency May Improve → If Auditor Stratifies a population → by dividing it into → Discrete Sub-Population → Which has an identifying characteristics
- (ii) Objective of stratification → To reduce variability of items → within each stratum group  
∴ Allows sample size to be reduced → without increasing sample risk
- (iii) If → CoT → A/c. Balance → Has been divided into station  
Projected misstatements from each station → Are Combined when considering the possible effect of Misstatement on Total → CoT → A/c. Bal.

## (B) Value Weighted Selection

- When Performing ToD → It may be efficient to identify sampling units as Individual Monetary units → That makes up the population
- Benefits : Sampling units Audit efforts is directed

↓  
To Larger Volume Items

↓  
Because

They have a greater chance of selection

They can be in smaller sample size

### Sample Size

- (1) The level of Sampling Risk → That Auditor is willing to accept  
↓  
Affects the sample size Required  
Lower Risk ↔ Greater Sample Size & Vice - Versa
- (2) Sample size can be determined by → Statistically based formulae → Exercise of professional Judgement
- (3) When circumstances are similar → The effect on sample size of factors → which have an effect on determination of sample size → will be similar in → Statistical → Non-Statistical → Approach
- (4) Factors Affecting sample size for → ToC → ToD

### ToC

- 1) Greater RELIANCE → Greater extent of ToC  
ON I.C.
- 2) ↑ Tolerable Rate of DEVIATION → ↓ in sample size
- 3) ↑ Expected Rate of Deviation → ↑ Sample size
- 4) ↑ Desired level of Assurance → ↑ in sample size
- 5) ↑ Homogenous sampling units → NO EFFECT

### ToD

- 1) ↑ ROMM → ↑ Sample size

Ankit Mundra

Ankit Mundra

Ankit Mundra

- 2) ↑ Substantive Procedures → TOD → SP → ↓ Sample Size
- 3) ↑ Desired Assurance → ↑ Sample Size
- 4) ↑ Tolerable Misstatement → ↓ Sample Size
- 5) Stratification of Population → ↓ Sample Size
- 6) No. of sampling units → NEGLIGIBLE EFFECT

Ankit Mundra

Ankit Mundra

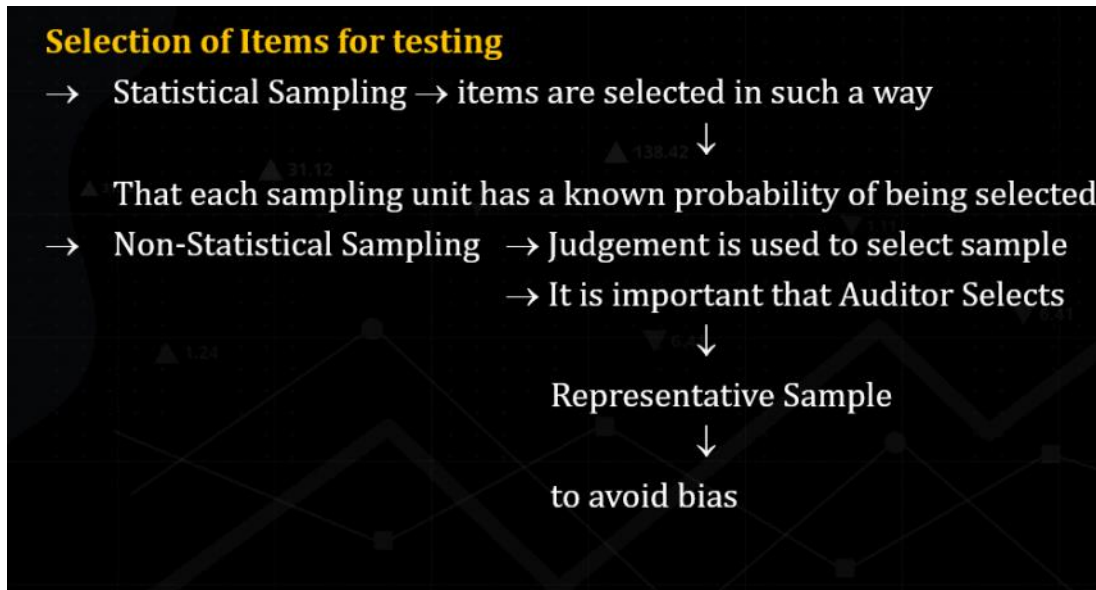
Ankit Mundra

Ankit Mundra

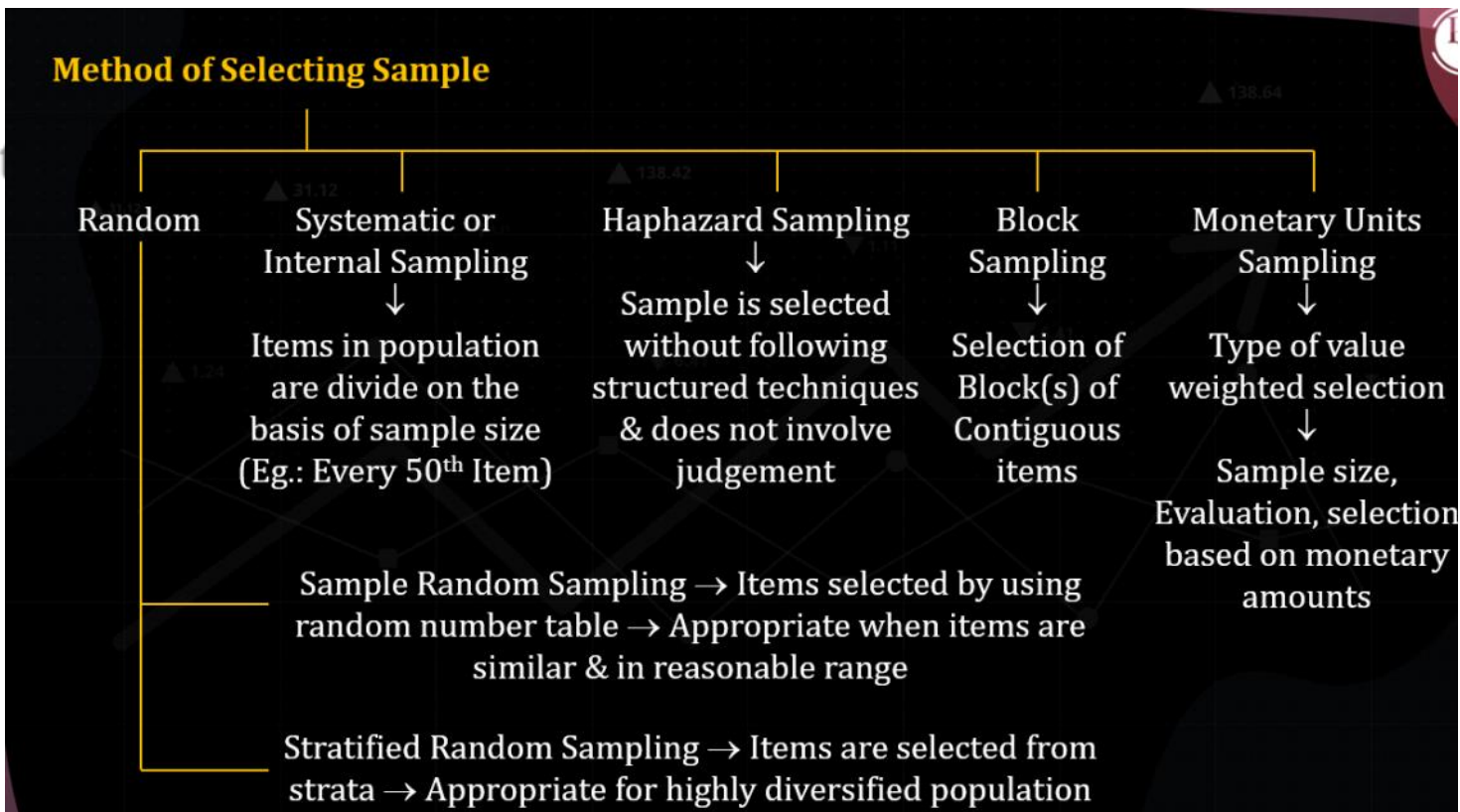
Ankit Mundra

Ankit Mundra

3.9.3 - Selection of Items for Testing



3.9.3A - Sample Selection Methods



3.10 - Performing Audit Procedures

**Performing Audit procedures**

- (1) Auditor should perform Audit procedures → Appropriate to the purpose → on each item selected
  - (2) If Audit procedure is → Not Applicable → Audit procedure is not be performed on → replacement Item
  - (3) If Auditor is unable to apply
    - ↓
    - On Selected items
    - ↓
    - The Auditor shall treat that item as
    - ↓
    - 'Deviation from prescribed control'
- Designed Audit procedure (Point-1)
- Suitable alternative procedure (Point-2)

## 3.11 - Nature and Cause of Deviations and Misstatements

**Nature & Cause of → Deviation & Misstatement**

In analyzing the → Deviations → Misstatements → identified



The Auditor may observe that → many have common features → then Auditor may

Identify all items in  
population

That possesses that  
common feature

∴ Auditor should

Extended Audit  
Procedures

To those items

Investigate → Nature & Causes of Deviations

Possible effects on Audit

May indicate the  
possibility of Fraud

Ank If Anomaly is discorsured → Obtain Certainty → Deviation → MM → not representative of population

May be excluded in projecting MM → However → Effects are to be considered → If uncorrected

3.12 - Projecting Misstatements

**Projecting Misstatements**

- The auditor is required to 'Project Misstatements → for the population
  - ↓
  - But this projection May not be sufficient
- When a misstatement has been established as an 'Anomaly'
  - ↓
  - It may be excluded when projecting misstatements
  - ↓
  - However its effects still needs to be considered
  - ↓

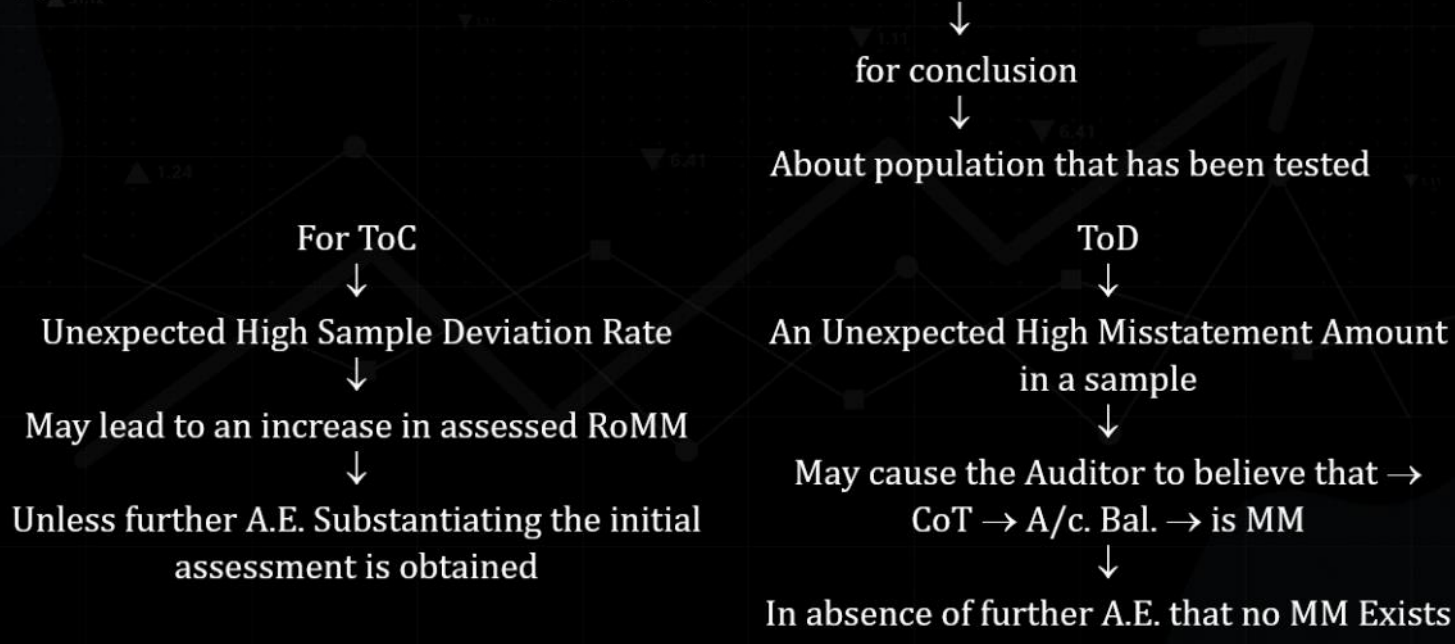
<ul style="list-style-type: none"> <li>➤ For ToC           <ul style="list-style-type: none"> <li>↓</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>ToD           <ul style="list-style-type: none"> <li>↓</li> </ul> </li> </ul>
Auditor shall → Project Misstatements	No Explicit projection of Deviation

3.13 - Evaluating Results of Audit Sampling

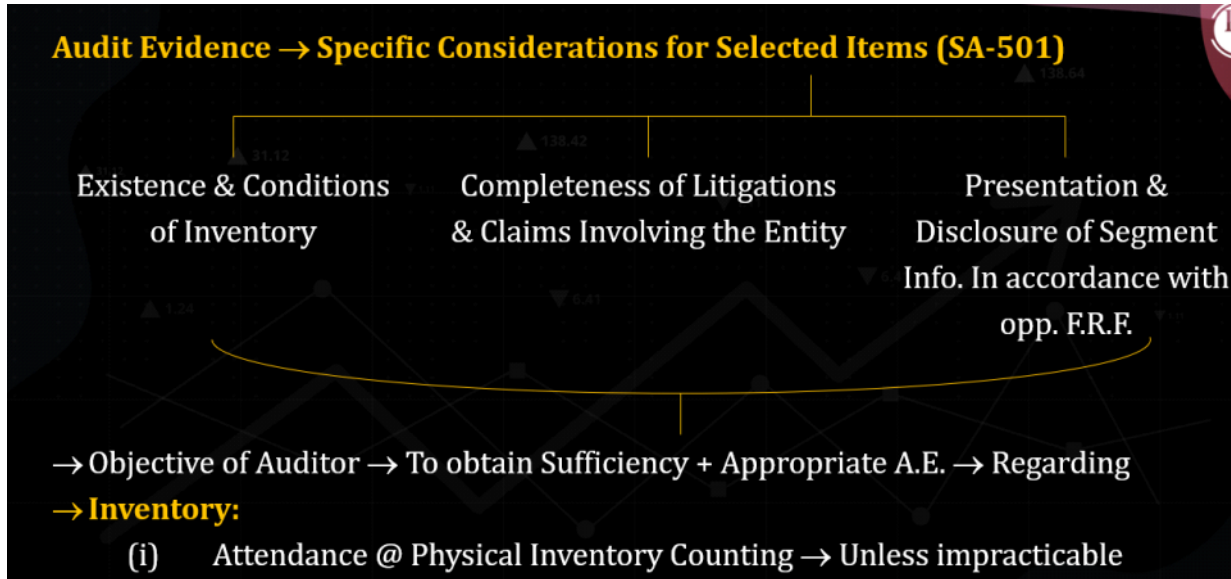
### Evaluating Result Audit Sampling

The Auditor shall Evaluate:

- (a) Result of Sample
- (b) Whether the use of Audit Sampling has provided a Reasonable Basis



4. - AUDIT EVIDENCE-SPECIFIC CONSIDERATIONS FOR SELECTED ITEMS  
(SA 501)



↳ Evaluate → Mgt.'s Instruction

↳ Observe → performance

↳ Inspect → Inventory

↳ Perform → Test Count

(ii) Performing Audit Procedures → Over Entity's Final Inventory Records

Attendance at Physical Inventory Counting Involves:

i) Inspecting → Existence  
→ Conditions  
→ perform → Test count

ii) Observing → compliance → Mgt. Instructions

iii) Obtaining → A.E. → Mgt. count procedure

4.5 - Matters Relevant in Planning Attendance at Physical Inventory Counting

### Matters Relevant to Planning Attendance @ Physical Inventory Counting

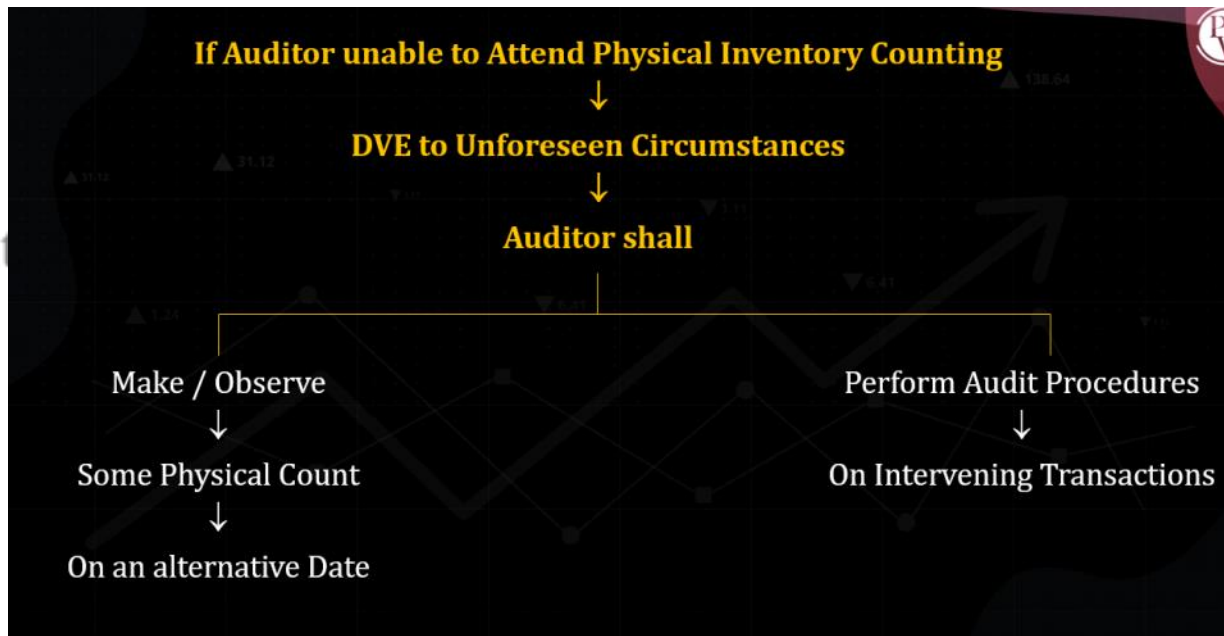
- Nature of Inventory
- Stages of W/P
- RoMM of Inventory
- Nature of IC
- Timing of Counting
- Entity Maintains → Perpetual Inventory System?

#### 4.6 Physical Inventory Counting Conducted other than at the Date of the Financial Statements

##### Physical Inv. Counting → Other than the date of F.S

Auditor Shall → Perform → Above Mentioned Audit Procedure + Additional Audit procedures to obtain Sufficiency + Appropriate A.E. about  $\Delta$  in Inventory

#### 4.7 If the auditor unable to Attend Physical Inventory Counting due to Unforeseen Circumstances



#### 4.8 Attendance at Physical Inventory Counting becomes impractical

##### Attendance of Physical Inventory is Impracticable

Auditor Shall:

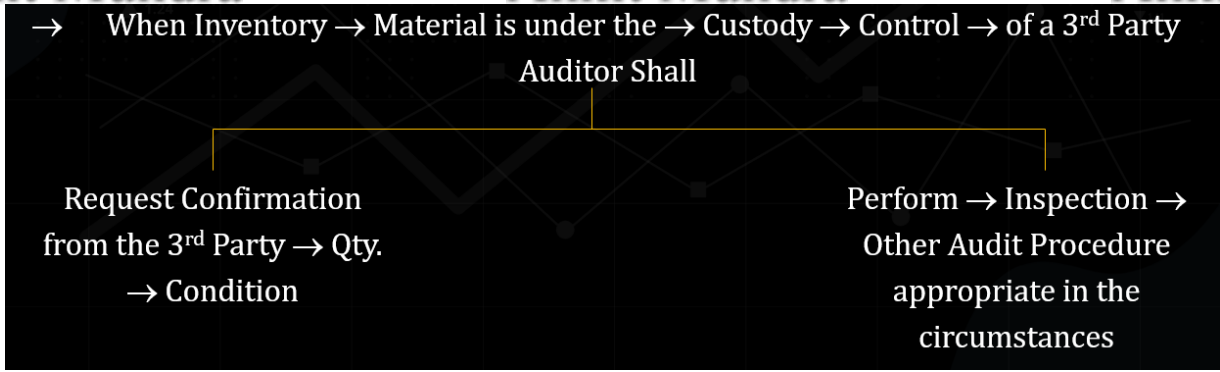
(i) Perform → Alternative Audit Procedure



If not possible → Modify as per SA 705

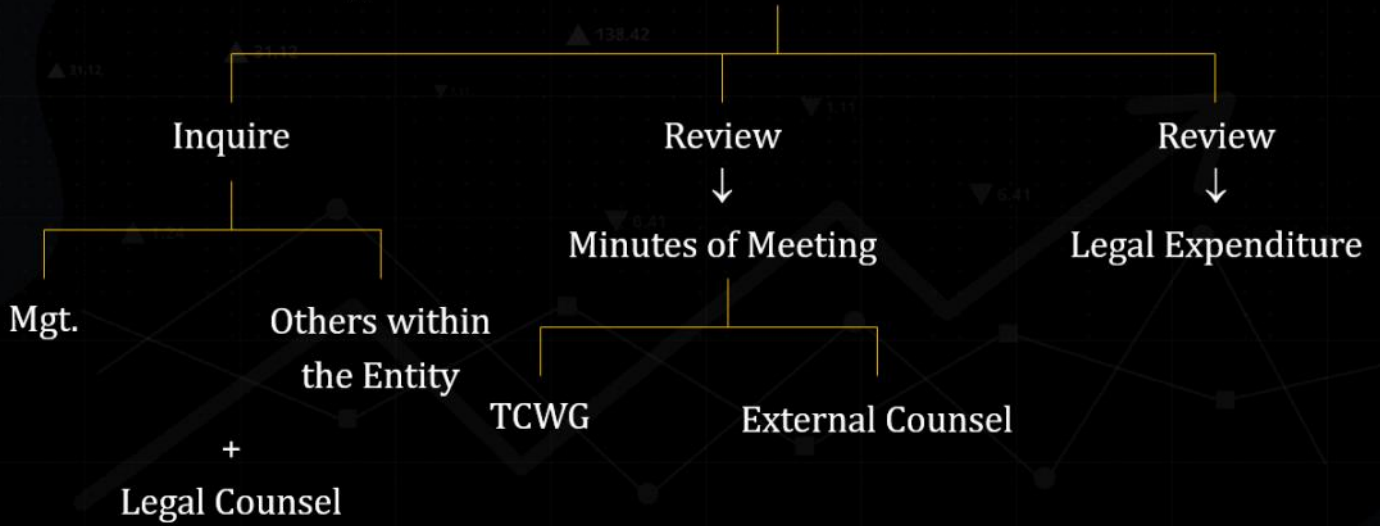
(ii) General Inconvenience to Auditor → Not sufficient Reason

#### 4.9 - When inventory under the custody and control of a third party- What will the auditor do?



**Litigation & Claims**

Auditor shall → Design → Perform ← Audit Procedures



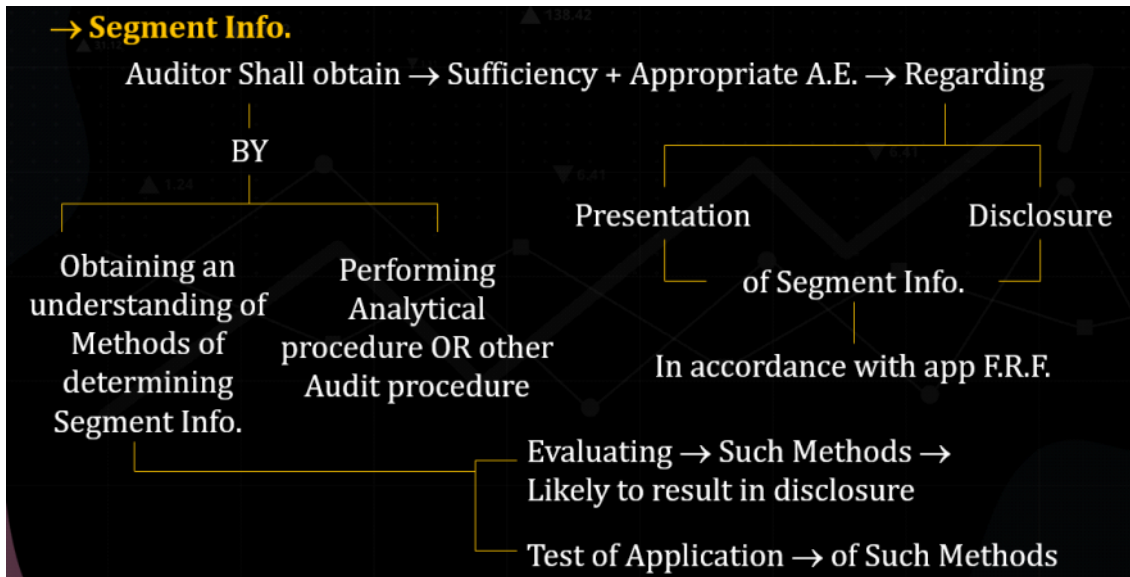
**If Auditor assess a RoMM → Regarding Litigation / Claim**

Communication with Entity's External Legal Counsel



→ Request W.R. → Mgt. → TCWG → that all → Known → Possible → Litigation have been disclosed

4.12 - Segment Information



4.14 - Auditor's responsibility regarding the presentation and disclosure of segment information

↓

Not required → to perform → Audit Procedures

↓

on STAND ALONE Basis

4.15 Understanding of the Methods Used by Management

**Methods used by Mgt.**

↓

Depends up on Circumstances

- Example of Methods
  - (i) Sales, Transfer, Elimination of Inter-Segment Amount
  - (ii) Comparison with Budgets
  - (iii) Allocation of → Assets → Costs → Amongst Segments
  - (iv) Consistency with prior periods

5. - EXTERNAL CONFIRMATIONS (SA 505)

**'External confirmation' SA 505**

↓

A.E. → Obtained as Direct Written Response → To the Auditor

↓

From a 3rd Party (Conforming Party)

↓

In

- Paper
- Electronic
- Other

Form

**Types of External confirmations**

- '+ve confirmation Request → Confirming Party Responds-Agrees/Disagrees
- '-ve confirmation Request → Confirming Party Responds → only when → Disagrees
- Non Response → failure to Respond
- Exception → Info  $\left\{ \begin{array}{l} \text{sought} \\ \text{obtained} \end{array} \right\}$  are different

5.5 - External Confirmation Procedures adopted by the Auditor to Obtain Audit Evidence

- i) Determine → Info. → to be  $\left\{ \begin{array}{l} \text{Confirmed} \\ \text{Requested} \end{array} \right\}$
- ii) selecting → Appro. confirming party
- iii) Designing → confirmation request
  - properly addressed
  - contain Return Info.

**Designing Confirmation Request : Factors to be considered**

- (i) Specified Identified RoMM → Including Fraud Risk
- (ii) The Layout & Presentation of Confirmation Request
- (iii) Prior Experience of Audit & Similar Engagements
- (iv) Mgt. → Authorization → Encouragement → to Confirming Party
- (v) The method of communication
- (vi) Ability of intended confirming Party → to confirm

iv) Sending the request + follow up

**Mgt's Refusal to allow the auditor to send a confirmation Request**

The Auditor shall :

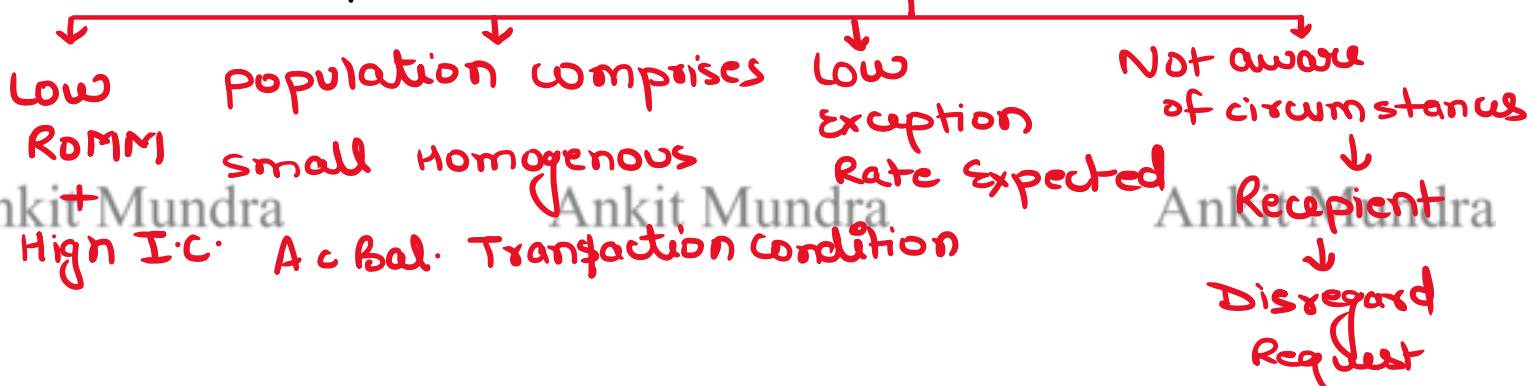
- (1) Inquire as to Mgt's → Reasons for Refusal + Seek A.E. → Validity → Reasonableness
- (2) Evaluate the implications → of Mgt's refused
- (3) Perform → Additional Audit Procedure

If Auditor concludes → Refusal → Unreasonable → Unable to obtain → Reliable → Relevant → A.E.

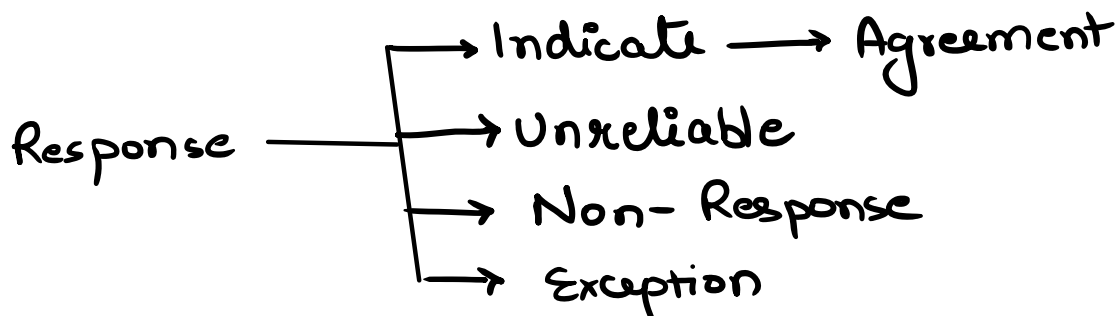
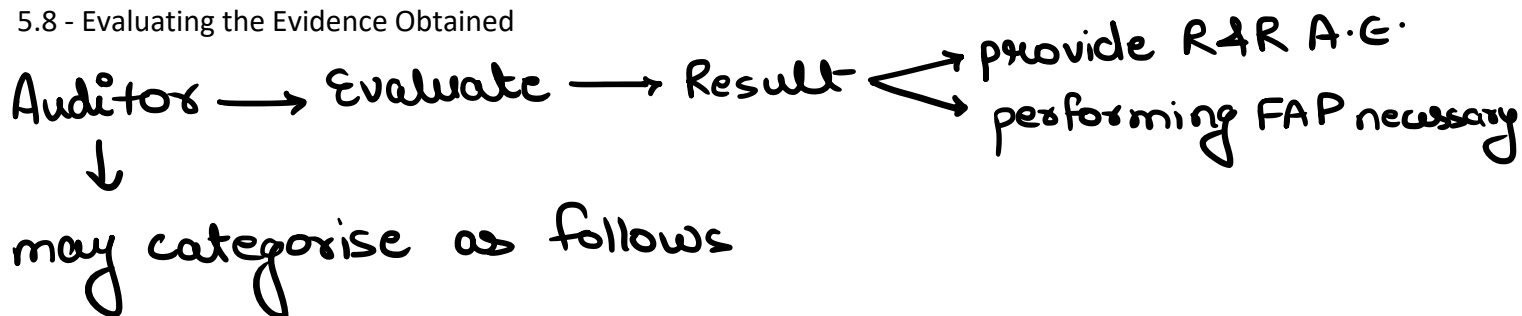
Communication with TCWG → as per SA 260

**\* Negative Confirmations**

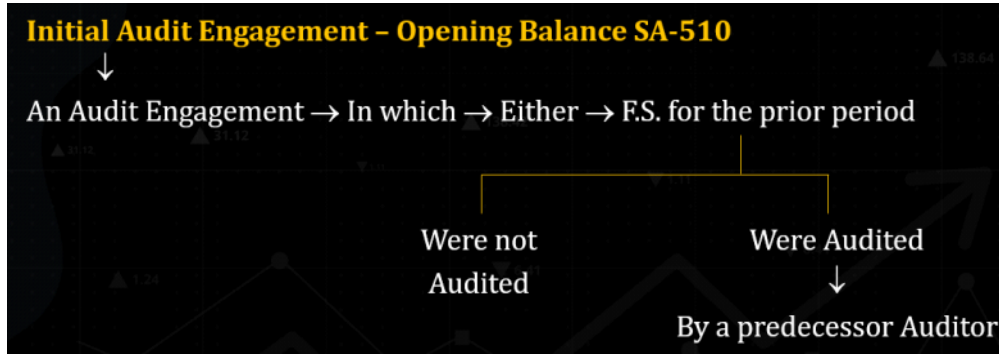
↳ Less persuasive than '+ve' confirmation

↳ Auditor SHALL NOT use as SOLE substantive procedure → **UNLESS:**

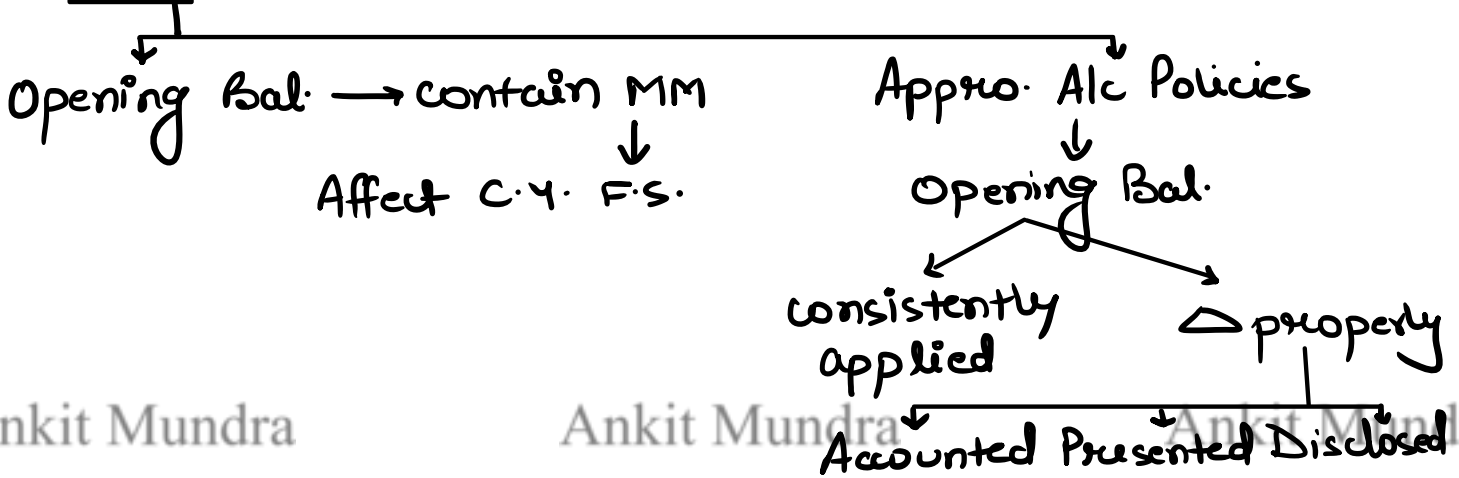
## 5.8 - Evaluating the Evidence Obtained



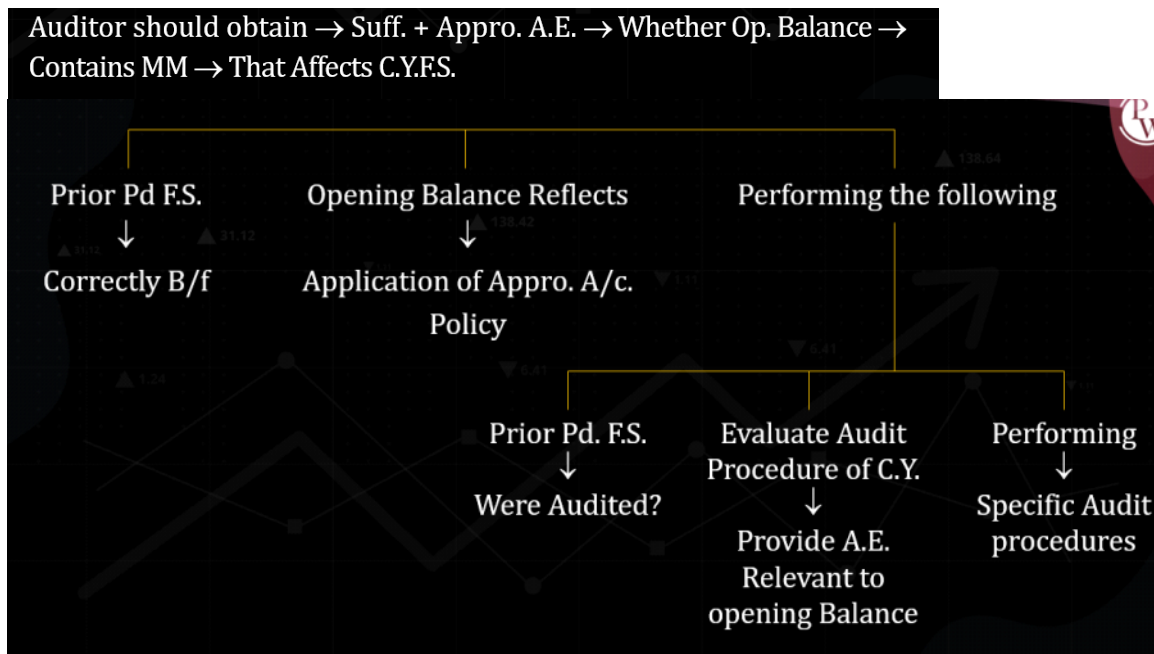
6. - INITIAL AUDIT ENGAGEMENTS - OPENING BALANCES (SA 510)



6.3 Objective of Auditor with respect to Opening Balances—in conducting an Initial Audit Engagement



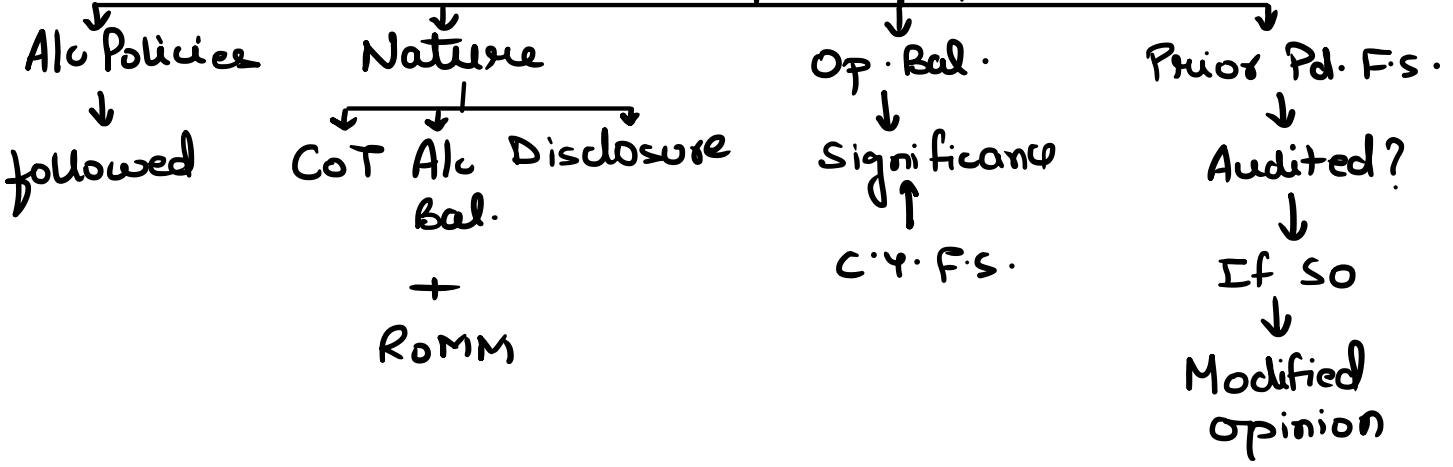
6.4 Obtaining sufficient appropriate Audit evidence about opening balances by the Auditor



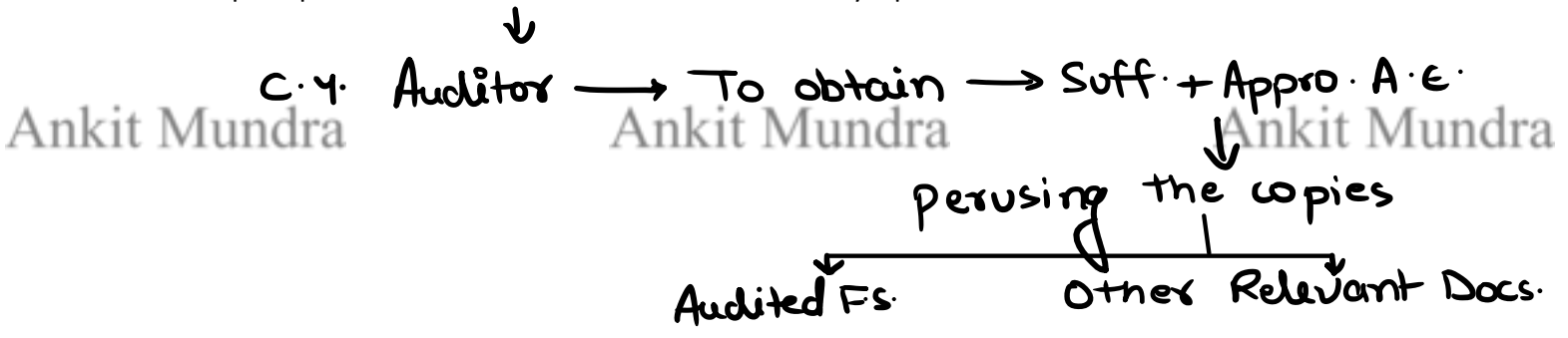
If misstatements are found → Communicate to Mgt./TCWG  
 ↓  
 As per SA 450 'Evaluating the Misstatement Identified during the Audit'

6.5 - Procedures adopted by the Auditor to Obtain Audit Evidence regarding opening balances:

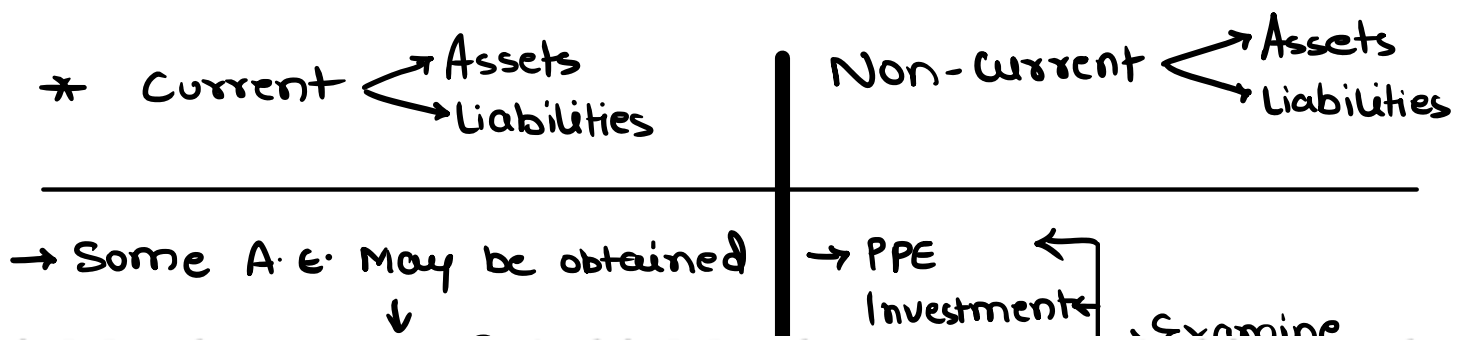
6.5.1 Nature and extent of Audit Procedures → Depends upon



6.5.2 - If the prior period's financial statements were audited by a predecessor auditor



\* Ordinarily → C.Y. Auditor → place reliance  
 ↓  
 Except  
 ↓  
 possibility of MM



→ Some A. E. May be obtained

↓  
C.Y. Audit Procedures

→ C.Y. Audit Procedures

↓  
provide little A. E.  
↓

Op. Inventory

→ Additional Audit Procedure

↳ Observe → physical count  
↳ Reconciliation

↳ valuation

↳ Audit Procedure → G.P. cut-off

→ PPE

Investment  
Long-Term  
Debt

Examine  
Alc  
Records  
Other  
Info.

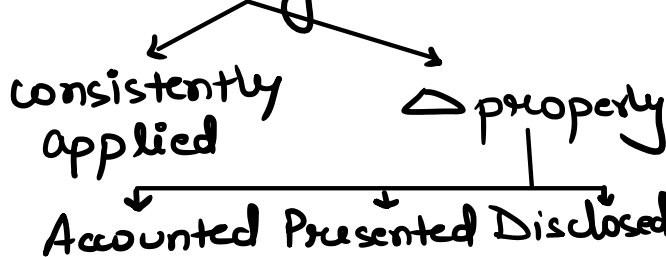
→ Certain cases

↓  
Through confirmation  
↓  
Third Parties

6.6 - Consistency of Accounting Policies relating to opening balances

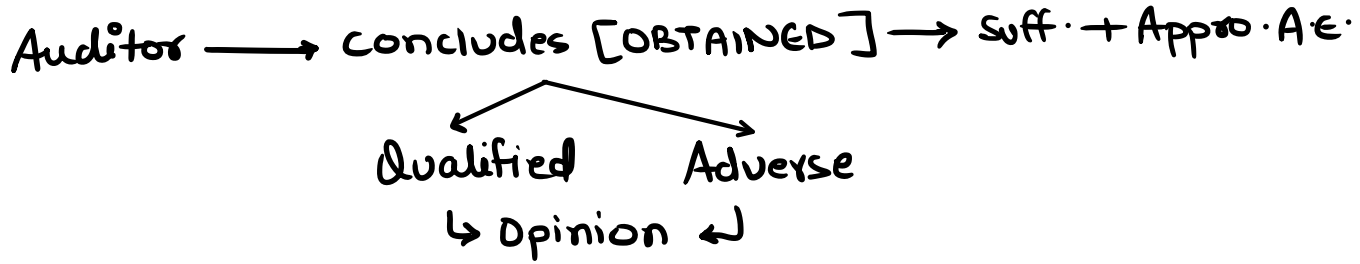
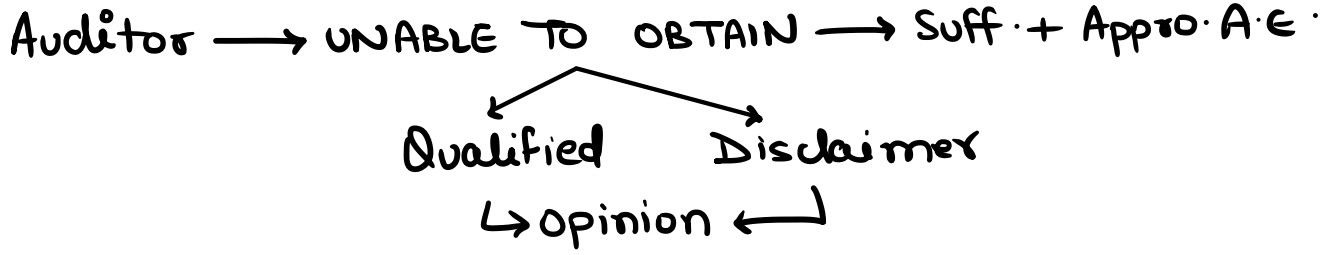
Appro. Alc Policies

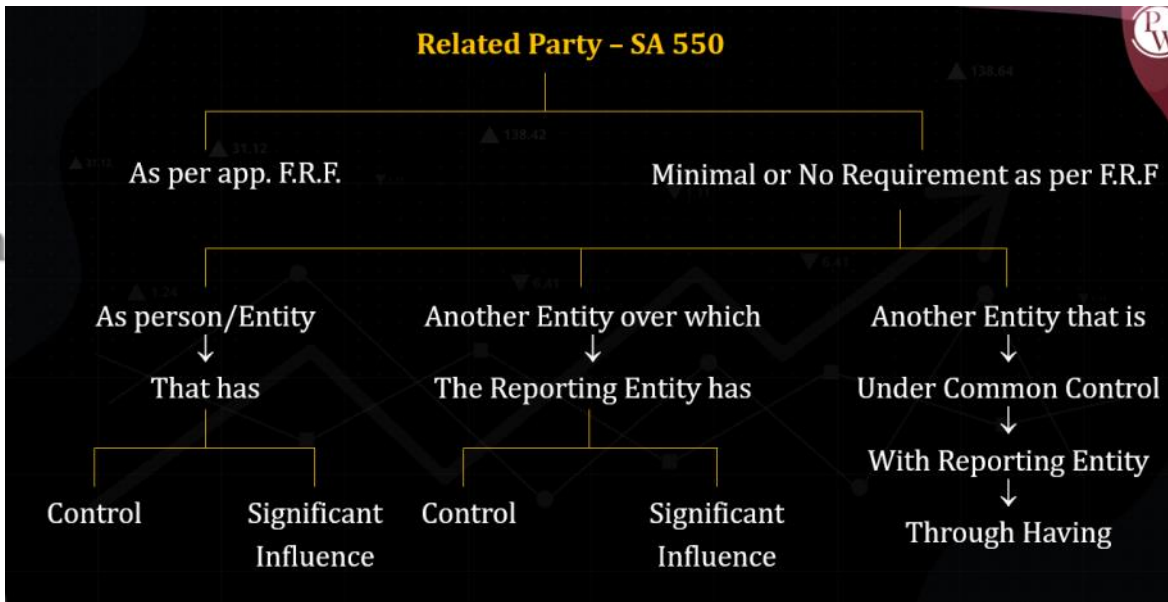
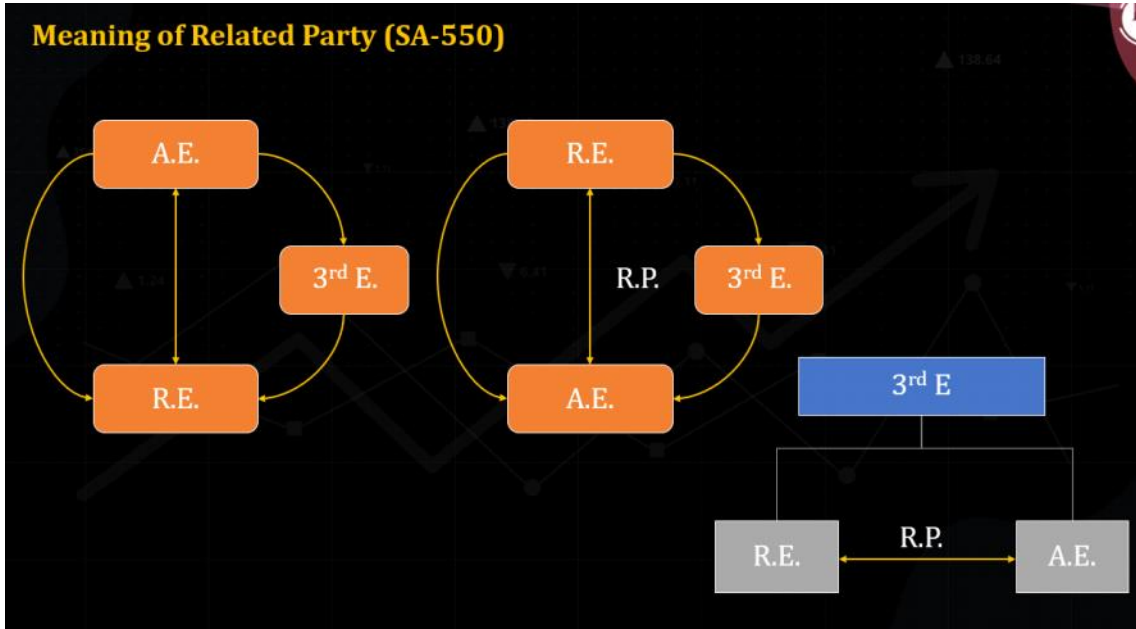
↓  
Opening Bal.

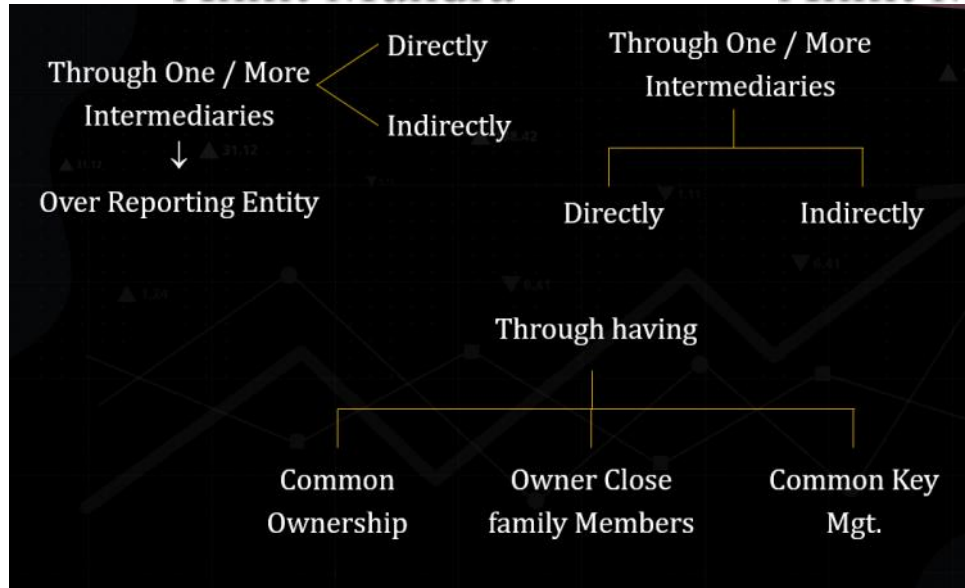


→ Auditor concludes → policies **NOT CONSISTENTLY APPLIED**  
 ↓  
 → Δ in policies **NOT PROPERLY ACCOUNTED**  
 ↓  
 Qualified / Adverse → Opinion → SA 705

6.7 Reporting by the auditor with regard to opening balances







7.3 Meaning of control and significant influence in reference to related party

Control → power to govern → Financial Operating policies of an Entity → To obtain Benefits from activities

Significant Influence → Gained by Ownership, Statute, Agreement → financial operating policies of an Entity

But NOT Control over those policies

\* Existence → of following Relationship → Indicate

- Control
- Significant Influence

- i) Direct > Equity Holding + Other Fin. Interest
- Indirect
- ii) Being part of → TCWG
- KMP
- iii) Close Family Members
- iv) Significant Business Relationship

7.4 Meaning of Related Parties with Dominant Influence (D.I.)

↓  
 may be in a position → to exert D.I. → Mgt. Entity

↓  
 should be considered → R.A.P. (SA 315)

7.5 Meaning of Special-Purpose Entities as Related Parties

↓  
 certain circumstances → may be Related Party

↓  
 Because the entity may → 'IN-SUBSTANCE' control it

↓  
 Even if owns → Little None > Equity

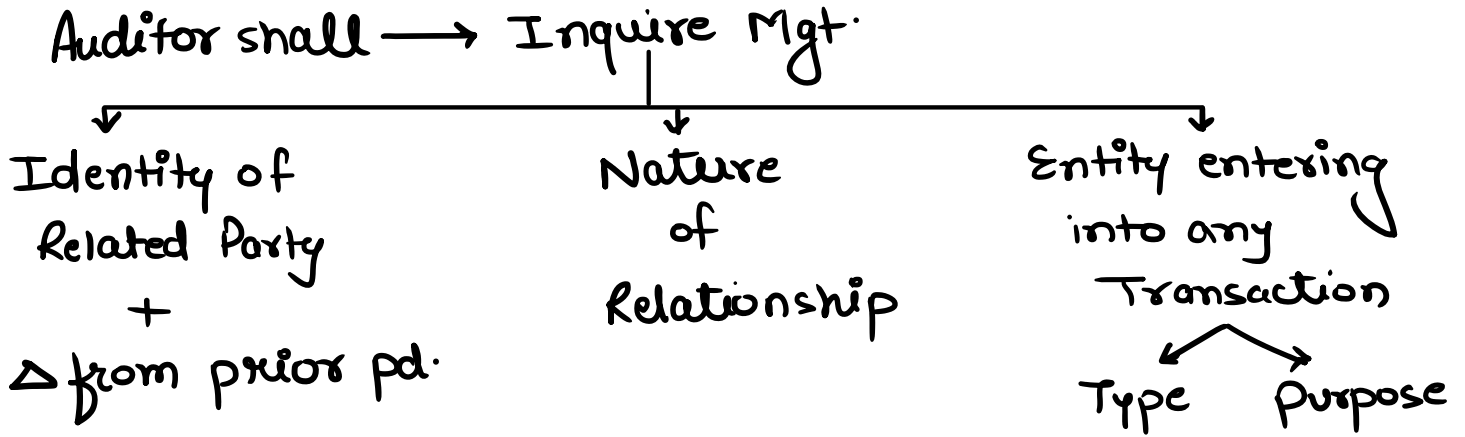
7.6 Nature of Related Party Relationships and Transactions

Many Related Party Transactions → Normal Course of Business

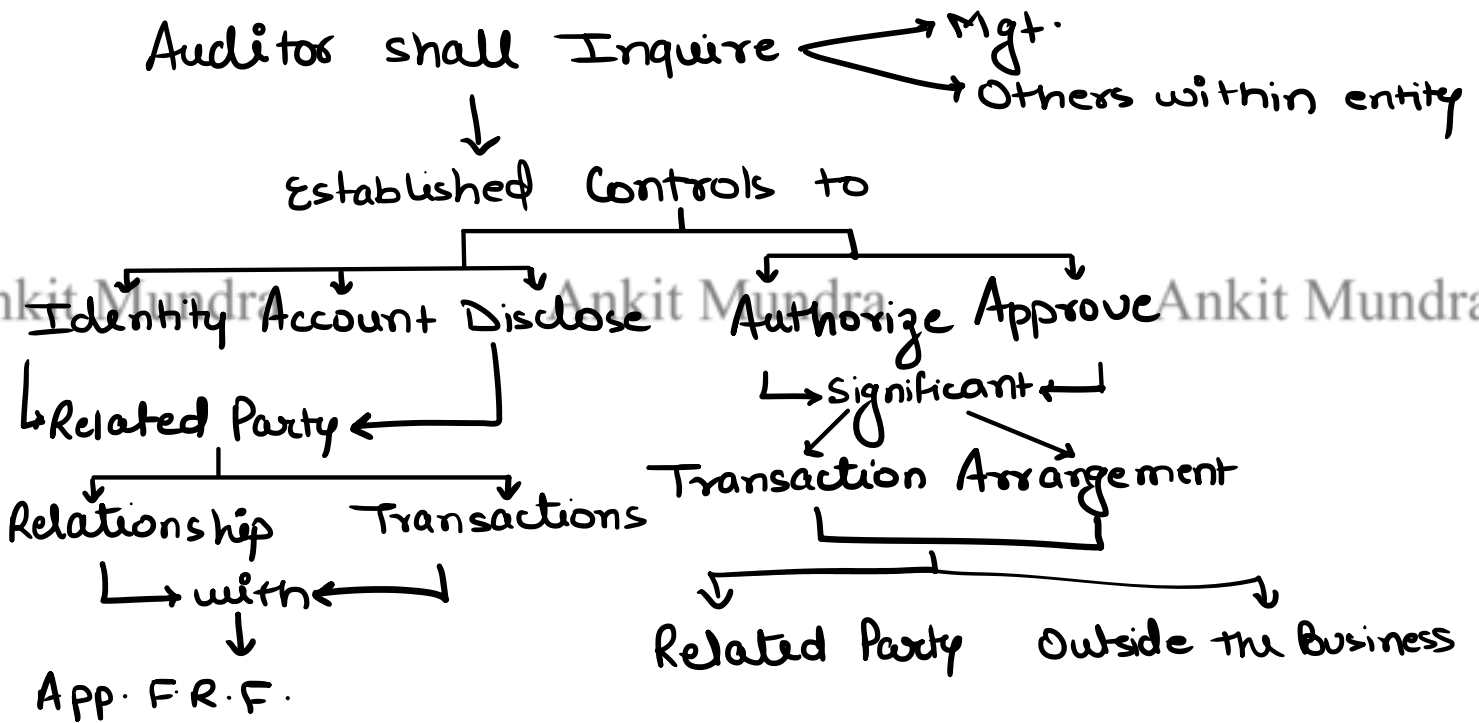
↓  
 May carry NO HIGHER RISK OF MM

7.7 Understanding the Entity's Related Party Relationships & Transactions

Auditor shall → Inquire Mgt.



\* Controls → for Related Party Transactions



7.8 Considerations specific to smaller entities by the auditor

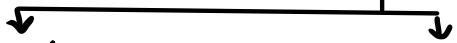
↓

Controls → Less Formal  
+  
No Documented Process  
+  
Increased Risk

→ Auditor may

i) Obtain understanding

→ Thorough



Related Party

Controls

Inquiry → Mgt.

Relationship Transactions

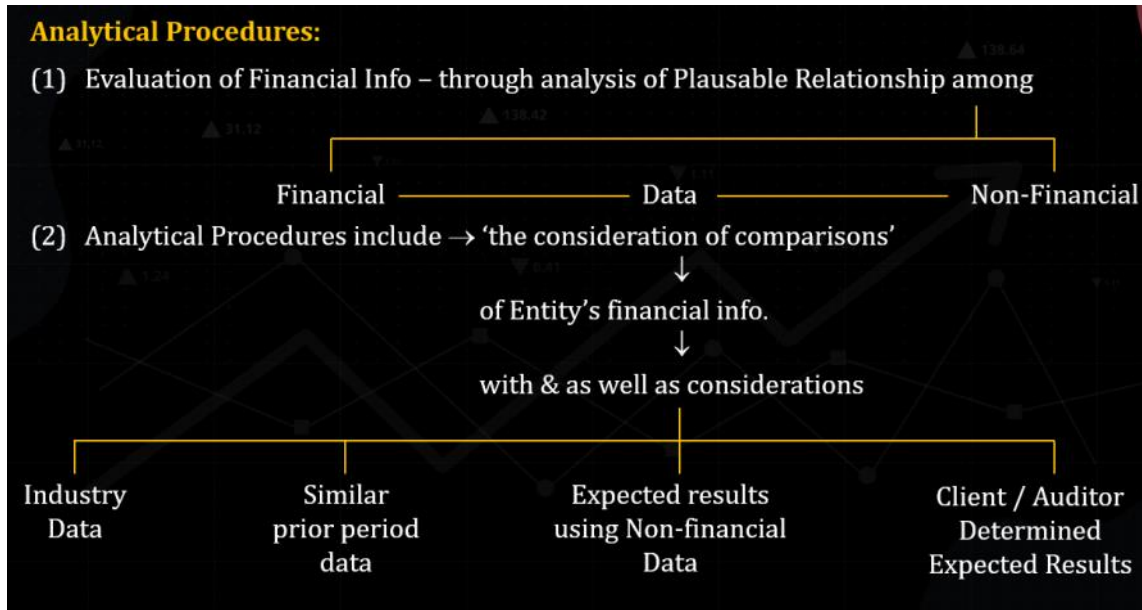
That may exist

Observation → Mgt.

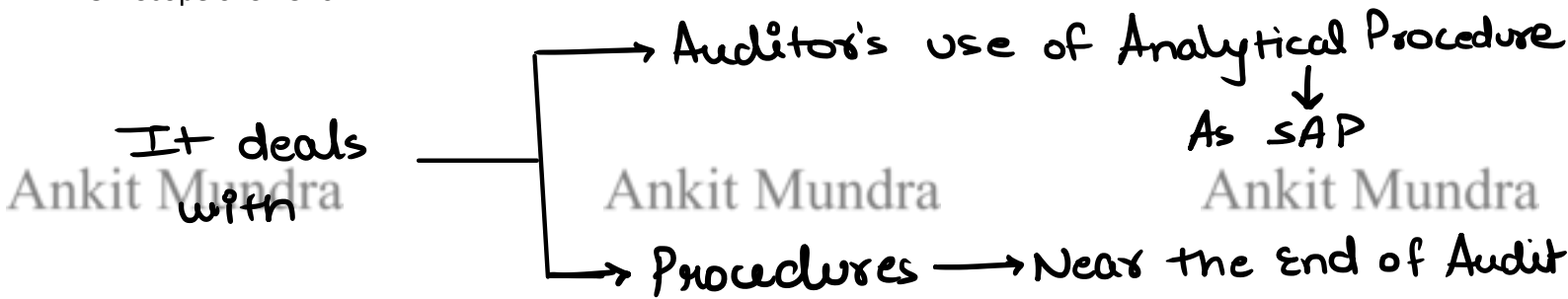
↓ Oversight Review

Inspection → Docs.

8. - ANALYTICAL PROCEDURES (SA520)



8.2 Scope of SA 520



**Objectives of SA-520**

- (1) To Obtain → Relevant → Reliable → A.E. → when using SAP
- (2) To → Design → Perform → Analytical Procedures → Near the end of Audit → to assist → in forming overall Audit Conclusion

**Purpose & Timing of Analytical Procedures**

(1) It was → Comparisons → Relationships → to assess → Reasonableness of Data

(2) These are helpful → in detection of

- Unusual State of affairs
- Mistakes in A/c.

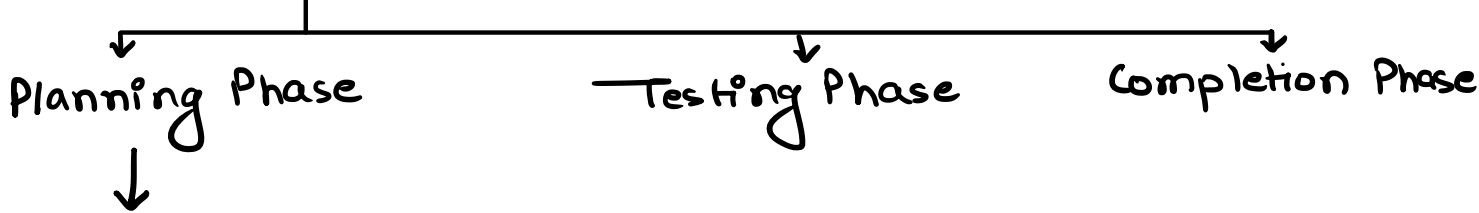
(3) The overall test can be extended for making → Inter → Infra → Firm Comparison → of trading result

(4) If MM are found → Auditor would

- Ascertain the reasons
- Assess whether A/c. has been manipulated

*(Note: A flowchart in the background shows 'Reasonableness of Data' branching into 'A/c. Bal.' and 'Other', and 'A/c. Bal.' further branching into 'Unusual State of affairs' and 'Mistakes in A/c.')*

Timing of Analytical Procedures



- ① understand  
↳ client Business
- ② Identify  
↳ potential Risk
- ③ Determine  
↳ N, E, T of other Audit Procedures
- ④ use  
↳ Fin. DATA  
↳ Non Fin INFO.

8.4 Substantive Analytical Procedures

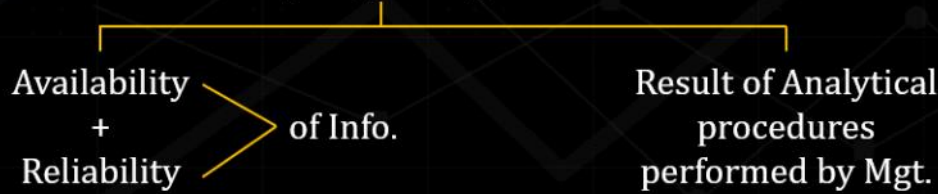
**Substantive Analytical Procedure (SAP)**

➤ Substantive Procedures @ Assertion Level



➤ Which procedure to perform → is based on Auditor's Judgement of Eff. & Eff. of → Available Audit procedures → to reduce risk @ acceptably low level

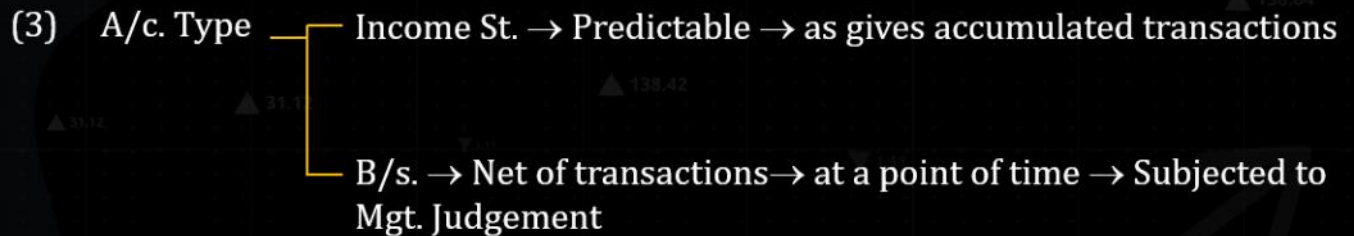
➤ Auditor may Inquire Mgt.



➤ Factors to be considered

(1) Availability of Data → Relevant & Reliable

(2) Disaggregation Breaking Down of Data → Degree of Disaggregation in available data



(4) Source → Some Sources (Routine) are better than others (Non-Routine) & SCoTs

(5) Predictability → Better

(6) Nature of Assertion → More evidence for assertions

(7) Inherent Risk or WCGW → Consider nature of RoMM in order to determine. If SAP can be used to obtain A.E.

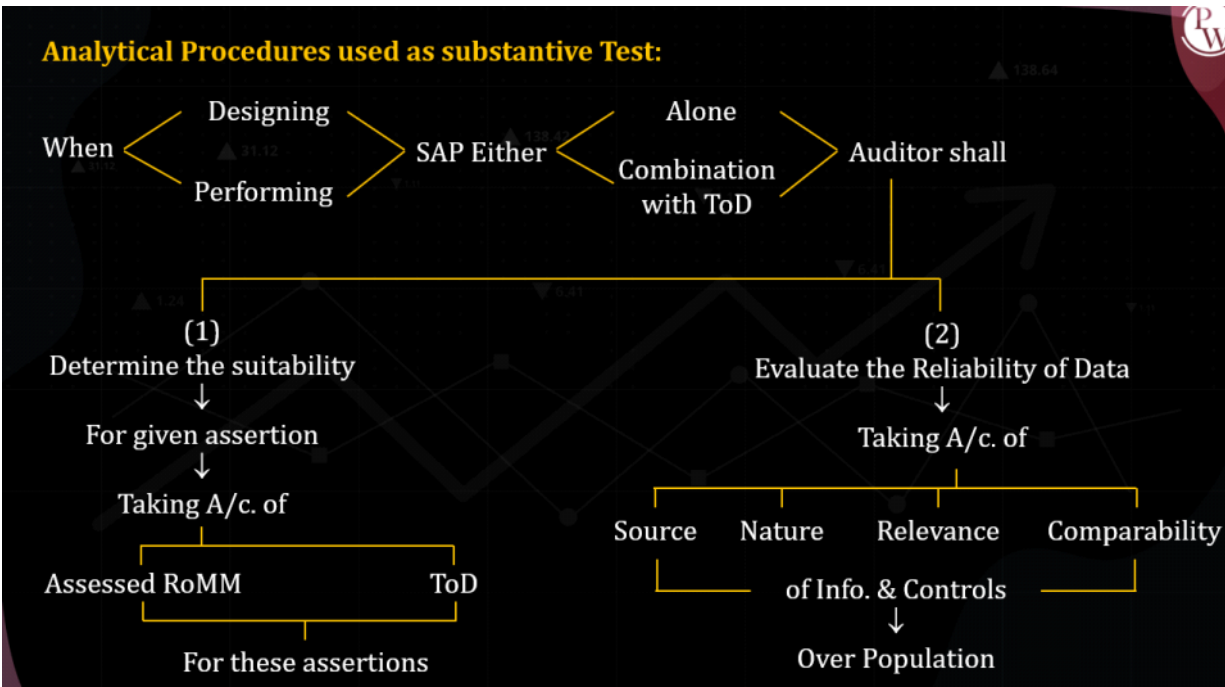
➤ When inherent Risk is Higher → ToD is to be designed

➤ When Significant Risk has been identified → A.E. from SAP unlikely to be sufficient

**Techniques available as SAP**

- (1) Trend Analysis → **commonly used technique**
- (2) Ratio Analysis
- (3) Reasonableness Test (Rely on Non-financial Data like interest rates to estimate interest incomes, etc.) → **unlike Trend Analysis**
- (4) Structural Modeling (Constructs a statistical Model from financial & Non-financial data of prior A/c. period to predict current A/c. Bal.)  
(Eg. Linear Regression)

8.7 - Analytical Procedures used as Substantive Tests



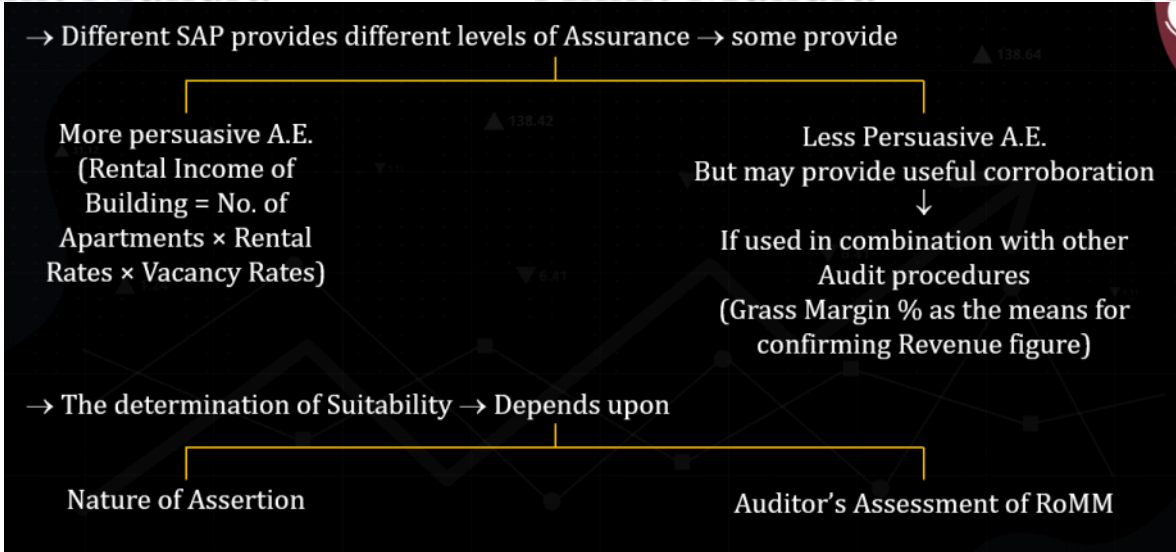
**1) Suitability of SAP for given assertion**

- SAP → generally more applicable to large volume of transaction → that tend to be predictable over time
- Applicability of SAP → is based on expectation that

```

    graph TD
        A[Relationship among Data Exists] --- B[Continue in absence of known conditions to the contrary]
    
```

- Suitability of SAP → depends upon Auditor's Judgement
- Sometimes 'unsophisticated predictive Model's → may be effective (No. of Employers × Rate / Employee = Total Payroll Cost)



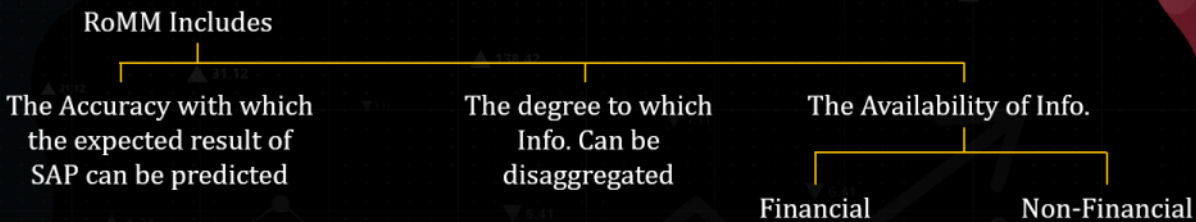
### 2) Extent of Reliance on Analytical Procedure

Following points are relevant for determining whether data is reliable for the purpose of designing SAP :

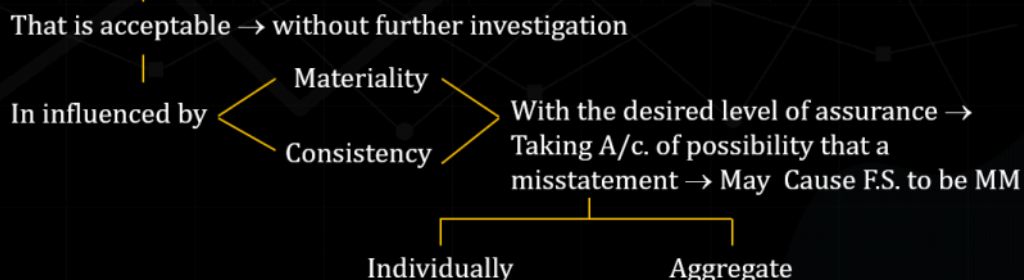
- (1) Source of Info. Available (more reliable if from Independent Source)
- (2) Comparability of Info. Available (Industry data may need to be supplemental to be comparable with Entity that sells Specialised products)
- (3) Nature & Relevance of Info. Available (Budgets have been established as a result to be expected rather than goals to be achieved)
- (4) Control over preparation of Info. → that are designed to ensure

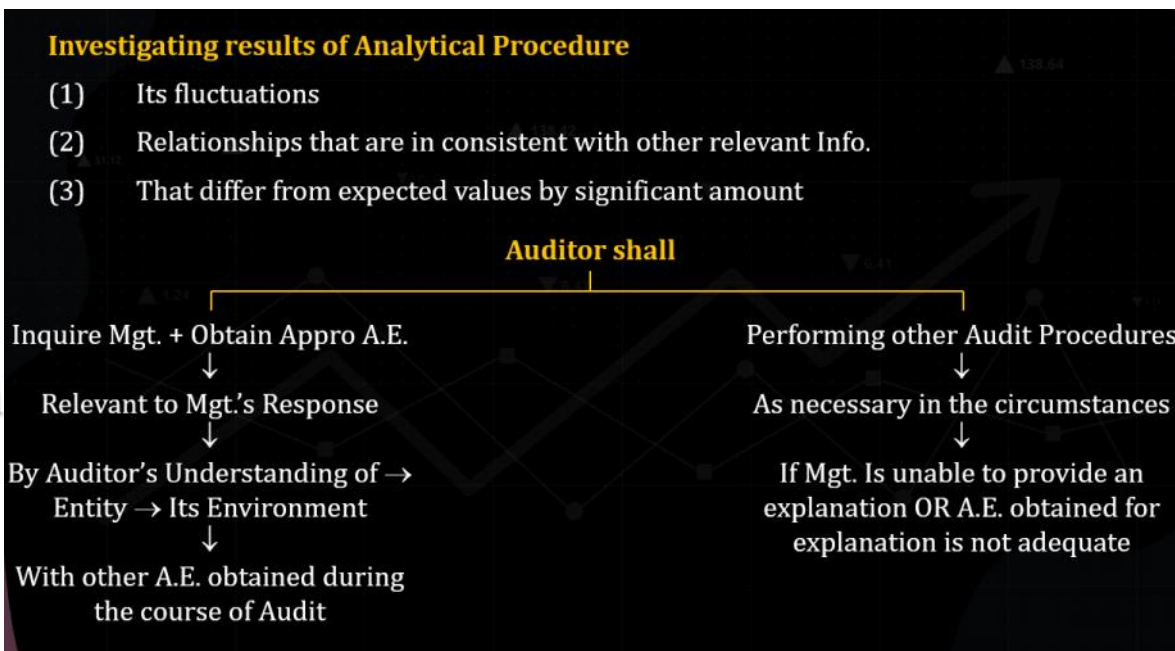
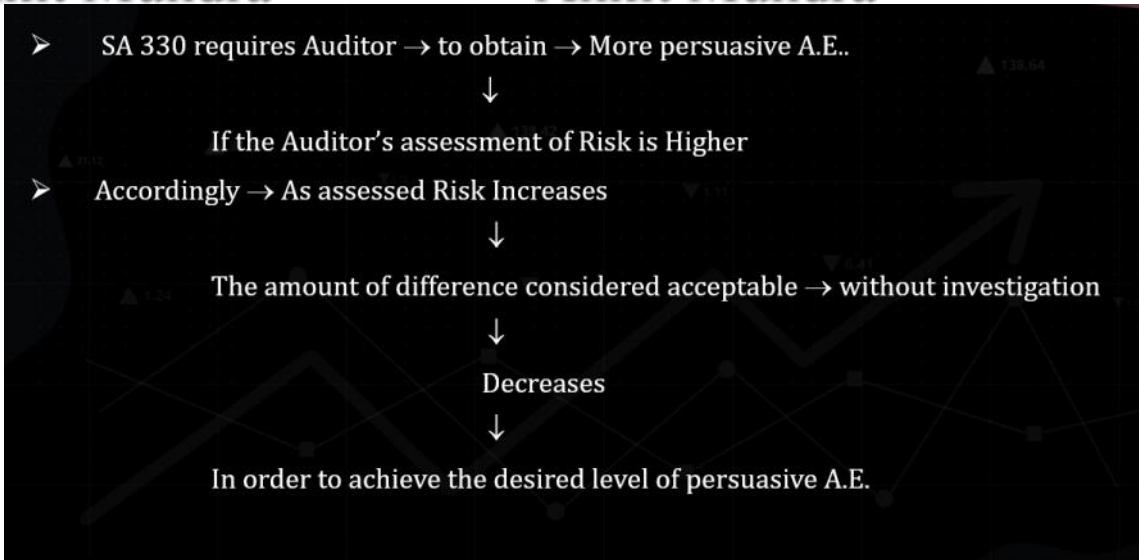


### (3) Evaluation of whether the expectation is sufficiently Precise

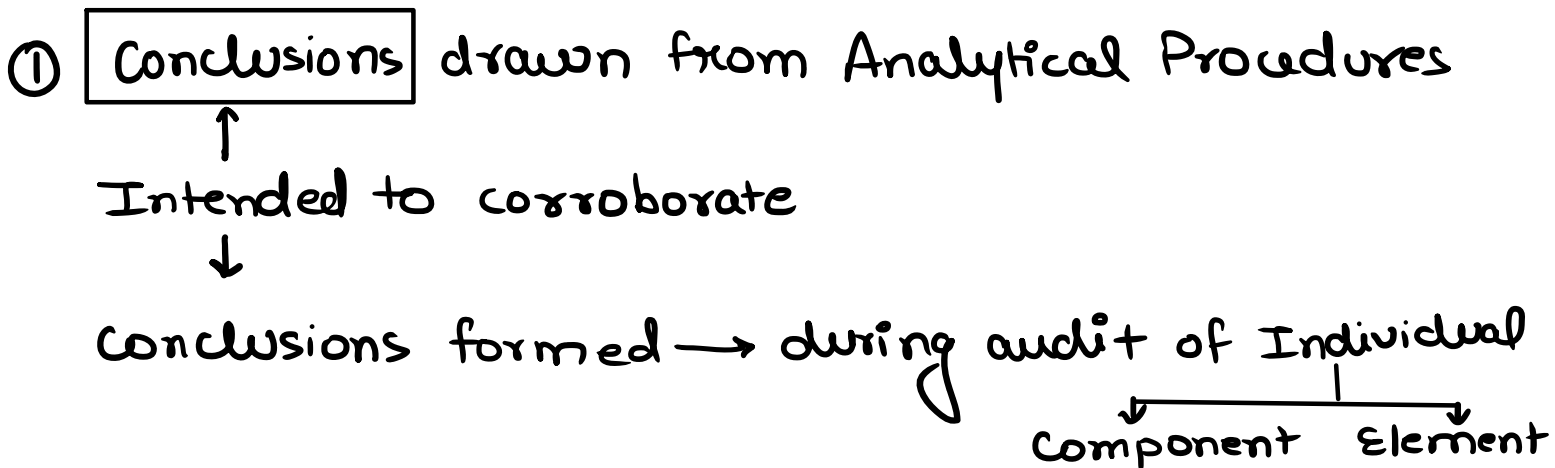


### (4) Amount of difference of Recorded Amounts → from → Expected Values





8.13 Analytical procedures that assist when forming an overall conclusion



② This assist Auditor → to draw → Reasonable Conclusion  
 ↓  
 on which to base Auditor's Opinion

③ The result of Analytical Procedure → may identify  
 ↓  
 previously unrecognised RoMM

