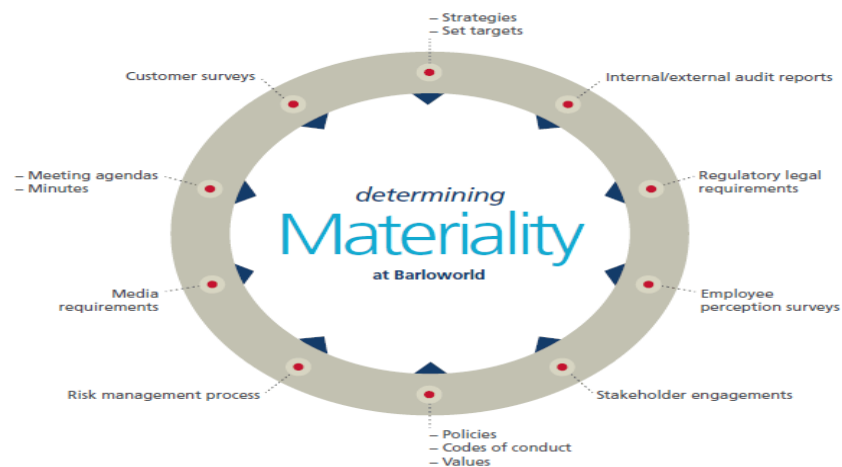


SA - 320

(REVISED) MATERIALITY IN PLANNING AND PERFORMING AN AUDIT

Scope of this SA

This Standard on Auditing (SA) deals with the auditor's responsibility to apply the concept of materiality in planning and performing an audit of financial statements. SA 450, explains how materiality is applied in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements.



Materiality in the context of an audit

1. Financial reporting frameworks often discuss the concept of materiality in the context of the preparation and presentation of financial statements. Although financial reporting frameworks may discuss materiality in different terms, they generally explain that:
 - a. Misstatements, including omissions, are material if they, individually or in the aggregate, influence the economic decisions of users taken on the basis of the financial statements;
 - b. Judgments about materiality are made in the light of surrounding circumstances, and are affected by the size or nature of a misstatement;; and
 - c. Judgments about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group.
2. If the applicable financial reporting framework does not include a discussion of the concept of materiality, the characteristics referred to in above paragraph provide the auditor with such a frame of reference.
3. The auditor's determination of materiality is a matter of professional judgment, and is affected by the auditor's perception of the financial information needs of users of the financial statements. In this context, it is reasonable for the auditor to assume that users:
 - a. Have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence;
 - b. Understand that financial statements are prepared, presented and audited to levels of materiality;
 - c. Recognize the uncertainties inherent in the measurement of amounts based on

	<p>the use of estimates, judgment and the consideration of future events; and</p> <p>d. Make reasonable economic decisions on the basis of the information in the financial statements.</p> <p>4. The concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report.</p> <p>5. In planning the audit, the auditor makes judgments about the size of misstatements that will be considered material. These judgments provide a basis for:</p> <p>(a) Determining the nature, timing and extent of risk assessment procedures;</p> <p>(b) Identifying and assessing the risks of material misstatement; and</p> <p>(c) Determining the nature, timing and extent of further audit procedures.</p> <p>The auditor considers not only the size but also the nature of uncorrected misstatements, when evaluating their effect on the financial statements.</p>
Effective date	This SA is effective for audits of financial statements for periods beginning on or after April 1, 2010.
Objective	The objective of the auditor is to apply the concept of materiality appropriately in planning and performing the audit.
Definition	For purposes of the SAs, performance materiality means the amount or amounts set by the auditor at less than materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. If applicable, performance materiality also refers to the amount or amounts set by the auditor at less than the materiality level or levels for particular classes of transactions, account balances or disclosures.
<p>Determining materiality and performance materiality when planning the audit</p> <p>Exam Nov 13; MTP Aug 18</p>	<p>1. When establishing the overall audit strategy, the auditor shall determine materiality for the financial statements as a whole. If there is one or more particular item for which misstatements of lesser amounts than the materiality for the financial statements as a whole could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements, the auditor shall also determine the materiality level or levels to be applied to those particular items.</p> <p>2. The auditor shall determine performance materiality for purposes of assessing the risks of material misstatement and determining the nature, timing and extent of further audit procedures.</p> <p>Use of Benchmarks in determining Materiality for the Financial Statements as a whole:</p> <p>Determining materiality involves the exercise of professional judgment. A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole. Factors that may affect the identification of an appropriate benchmark include the following:</p> <ul style="list-style-type: none"> • The elements of the financial statements (for example, assets, liabilities, equity, revenue, expenses); • Whether there are items on which the attention of the users of the particular entity's financial statements tends to be focused (for example, for the purpose of evaluating financial performance users may tend to focus on profit, revenue or net assets); • The nature of the entity, where the entity is at in its life cycle, and the industry and economic environment in which the entity operates; • The entity's ownership structure and the way it is financed (for example, if an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings); and