



# CA INTER AUDIT

NOV'23

## Chapter-2

# Audit Strategy, Planning and Programme

**QUESTION BANK**



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# Preface

## Greetings students,

As the author of this question bank, I've taken a thoughtful approach to its construction, prioritizing a competitive spirit in your learning journey.

## Dedication to Holistic Learning

My dedication to creating content knows no bounds. I've meticulously curated questions from over 20 years of ICAI materials, including Study Material Practice Questions, MTPs, RTPs, and Suggested Answers. The sequencing of chapter topics aligns seamlessly with the ICAI study material.

## Correct / Incorrect Questions

The Correct and Incorrect questions/answers are intentionally not kept in sequential order. Why? To encourage analytical thinking without the comfort of knowing the topic heading in advance.

## Insights from Examiner Comments

Moreover, the inclusion of examiner comments adds a unique dimension. Learning from the mistakes highlighted by ICAI examiners can significantly improve your understanding. This book is not just about questions and answers; it's a tool to help you comprehend common mistakes and guide you on how to avoid and rectify them.

## Comprehensive Question Selection Strategy

I've gone a step further. Not only have I kept questions directly related to the current study material, but I've also included additional ones related to previous years with some relevance to the current context. These carry relevance, but I advise focusing on them only after thoroughly covering the main syllabus according to the current study material.

## Video Learning Initiative



And here's an exciting initiative—I've started creating YouTube videos to help you understand any challenging question or topic. All you need to do is message us on WhatsApp or Telegram using the provided link at the bottom of the page, and I'll promptly create a video to address your request.

## Closing Note: Embark on Your Learning Journey

So, dive into this question bank with enthusiasm, and remember, I'm here to support your learning journey every step of the way.

Best regards,  
Prof. Vishal Atman

**If you require further assistance with your study techniques or any other aspect, don't hesitate to contact us.**

You can instantly reach out via WhatsApp by clicking this icon,  or join our Telegram group  to pose questions that could also benefit your peers.



<h1 style="margin: 0;">Chapter 2</h1>	<h1 style="margin: 0;">Audit Strategy, Planning And Programme</h1>
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## Part A – Correct Incorrect

Q. 1 State with reasons (in short) whether the following statements are True or False :	
1.	<p><b>There is no relation between Audit Plans and knowledge of the client’s business</b></p> <p style="text-align: right;">(RTP IPCC Nov 18)</p>
	<p><b>Incorrect</b></p> <p>The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client’s business</p>
2.	<p><b>Establishing an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan is prerogative of the management.</b></p> <p style="text-align: right;">(TYK)</p>
	<p><b>Incorrect</b></p> <p>The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. It’s the responsibility of an Auditor and not the right of management.</p>
3.	<p><b>The audit plan is more detailed than the overall audit strategy.</b></p> <p style="text-align: right;">(2 Marks) (Audit / Nov. 2020)</p>
	<p><b>Correct</b></p> <p>The audit plan is more detailed than the overall audit strategy that includes the nature, timing and extent of audit procedures to be performed by engagement team members. Once the overall audit strategy has been established, an audit plan can be developed to achieve the audit objectives through the efficient use of the auditor’s resources.</p>
4.	<p><b>Development of an audit plan is important before the establishment of the overall audit strategy to address the various matters.</b></p> <p style="text-align: right;">(Inter RTP Nov.2022)</p>
	<p><b>Incorrect:</b></p> <p>As per SA-300, “Planning an Audit of Financial Statements”, the auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. Once the overall audit strategy has been established, an audit plan can be developed to address the various matters identified in the overall audit strategy, taking into account the need to achieve the audit objectives through the efficient use of the auditor’s resources.</p>
5.	<p><b>Planning is a discrete phase of an audit.</b></p> <p style="text-align: right;">(MTP May 2023) (2 Marks each, RTP Nov 17) (RTP IPCC Nov 19)</p>
	<p><b>Incorrect</b></p> <p>According to SA-300, “Planning an Audit of F.St.’s”, planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement. Planning, however, includes consideration of the timing of certain activities and audit procedures that need to be completed prior to the performance of further audit procedures.</p>



6.	<p><b>Planning is not a discrete phase of an audit, but rather a continual and iterative process.</b></p> <p style="text-align: right;">(RTP IPCC Nov 18)</p> <p><b>Correct</b></p> <p>According to SA-300, "Planning an Audit of F.St.'s", planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement. Planning, however, includes consideration of the timing of certain activities and audit procedures that need to be completed prior to the performance of further audit procedures.</p>
7.	<p><b>The auditor need not discuss elements of planning with the entity's management in any case.</b></p> <p style="text-align: right;">(RTP IPCC Nov 19)</p> <p><b>Incorrect</b></p> <p>The auditor may decide to discuss elements of planning with the entity's management to facilitate the conduct and management of the audit engagement.</p>
8.	<p><b>The auditor shall update and change the overall audit strategy and the audit plan as necessary during the course of the audit.</b></p> <p style="text-align: right;">(MTP Aug-New 2018, 2 Marks)</p> <p><b>Correct</b></p> <p>The auditor shall update and change the overall audit strategy and the audit plan as necessary during the course of the audit. As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan and thereby the resulting planned nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks.</p>
9.	<p><b>A well designed and drafted audit plan and audit strategy which takes care of all the uncertainties and conditions, need not be changed during the course of audit.</b></p> <p style="text-align: right;">(2 Marks, Nov 2018)</p> <p style="text-align: center;">OR</p> <p><b>Once the audit plan has been drafted and communicated, it is obligatory on the auditor to follow the same.</b></p> <p style="text-align: right;">(MTP May 2023)</p> <p><b>Incorrect</b></p> <p>The auditor shall update and change the overall audit strategy and the audit plan as necessary during the course of the audit. As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan and thereby the resulting planned nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks.</p> <p><b>Examiner Comment - Few examinees did not mention that as a result of unexpected events, changes in condition, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall strategy and audit plan.</b></p>
10.	<p><b>A detailed Audit Programme once prepared for a business can be used for all business under all circumstances.</b></p> <p style="text-align: right;">(MTP Oct 2020, 2 Marks) (2 Marks, MTP Oct.,2022)</p> <p style="text-align: center;">OR</p> <p><b>Evolving one audit programme applicable to all business under all circumstances is not practicable.</b></p> <p><b>Correct</b></p> <p>Businesses vary in nature, size and composition; work which is suitable to one business may not be suitable to others; efficiency and operation of internal controls and the exact nature of the service to be rendered by the auditor are the other factors that vary from assignment to assignment. On account of such variations, evolving one audit programme applicable to all business under all circumstances is not practicable</p>
11.	<p><b>The "documentation of the overall audit strategy" is a record of the audit evidences considered necessary to properly plan the audit and to assign various audit functions to the engagement team.</b></p> <p style="text-align: right;">(Inter Sugg. 2023)</p>

12.	<p><b>Incorrect :</b></p> <p>The documentation of the overall audit strategy is a record of the key decisions considered necessary to properly plan the audit and to communicate significant matters to the engagement team. Example: The auditor may summarize the overall audit strategy in the form of a memorandum that contains key decisions regarding the overall scope, timing and conduct of the audit.</p>
13.	<p><b>It is not necessary for the auditor to periodically review the audit programmed.</b></p> <p style="text-align: right;">(2 Marks) (Audit / Nov. 2020)</p> <p><b>Incorrect</b></p> <p>There should be periodic review of the audit programmed to assess whether the same continues to be adequate for obtaining requisite knowledge and evidence about the transactions. Unless this is done, any change in the business policy of the client may not be adequately known, and consequently, audit work may be carried on, on the basis of an obsolete programmed and for this negligence, the whole audit may be held as negligently conducted and the auditor may have to face legal consequences.</p>
14.	<p><b>Under a properly framed audit programme by the auditor, the danger is significantly less and audit can proceed systematically.</b></p> <p style="text-align: right;">(2 Marks, Nov 2019 – Inter New)</p> <p><b>Correct :</b> Without a written and pre-determined programme, work is necessarily to be carried out on the basis of some 'mental' plan. In such a situation there is always a danger of ignoring or overlooking certain books and records. Thus, under a properly framed programme, the danger is significantly less and the audit can proceed systematically.</p>
15.	<p><b>Materiality is not a matter of size.</b></p> <p style="text-align: right;">MTP May 2023</p> <p><b>Incorrect:</b></p> <p>Financial statements should disclose all 'material items', i.e., the items the knowledge of which might influence the decisions of the user of the financial statement. Materiality is not always a matter of relative size. For example -a small amount lost by fraudulent practices of certain employees can indicate a serious flaw in the enterprise's internal control system requiring immediate attention to avoid greater losses in future. In certain cases, quantitative limits of materiality are specified.</p>
16.	<p><b>If during the audit it appears as though actual financial results are likely to be substantially different from the anticipated period end financial results that were used initially to determine materiality for the financial statements as a whole, the auditor revises that materiality.</b></p> <p style="text-align: right;">(2 Marks, MTP Oct.,2022)</p> <p><b>Correct</b></p> <p>Materiality for the financial statements as a whole (and, if applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures) may need to be revised as a result of a change in circumstances that occurred during the audit, new information, or a change in the auditor's understanding of the entity and its operations as a result of performing further audit procedures.</p>
17.	<p><b>The utility of the audit programme can be retained and enhanced only by keeping the programme and also the client's operations and internal control under periodic review so that inadequacies or redundancies of the programme may be removed'. Discuss stating clearly the advantages of an audit programme.</b></p> <p style="text-align: right;">(TYK)</p> <p><b>Incorrect</b></p> <p>Materiality for the financial statements as a whole (and, if applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures) may need to be revised as a result of a change in circumstances that occurred during the audit (for example, a decision to dispose of a major part of the entity's business), new information, or a change in the auditor's understanding of the entity and its operations as a result of performing further audit procedures.</p>



18. **When Profit before tax from continuing operations is non-volatile, other benchmarks will be appropriate.**

(Inter Audit Suggested / New Dec. 2021)

**Incorrect**

Profit before tax from continuing operations is often used for profit-oriented entities. When profit before tax from continuing operations is volatile, other benchmarks may be more appropriate, such as gross profit or total revenues.

## OLD Course SM

19. **The concept of materiality is an important and relevant consideration for the auditor in financial statement.**

(OLD Course SM) (2 Marks, Nov 2018) (2 Marks, MTP Sep.2022)

**Correct**

The concept of materiality is fundamental to the process of accounting. It covers all the stages from recording to classification and presentation. It is very important for the auditor who has constantly to judge whether a particular item is material or not and ensure that a material item is disclosed separately and distinctly.

Examiner Comment - Examinees explained that it is fundamental to the process of accounting but did not discuss appropriately the need for separate disclosure of material items.

20. **When inherent and control risks are low, an auditor can accept a lower detection risk.**

(OLD Course SM) (2 Marks each, May 2008)

**False :**

SA-320 on "Materiality in Planning and Performing an Audit" states that the auditor obtains reasonable assurance by obtaining sufficient appropriate audit evidence to reduce audit risk to an acceptably low level. After the auditor assesses the inherent and control risks, he should consider the level of detection risk that he is prepared to accept and, based upon his judgment, select appropriate substantive audit procedures. If the auditor does not perform any substantive procedures, detection risk, that is, the risk that the auditor will fail to detect a misstatement, will be high. The auditor reduces detection risk by performing substantive procedures - the more extensive the procedures performed, the lower the detection risk.

21. **There is direct relationship between materiality and the degree of audit risk.**

(OLD Course SM) (RTP IPCC May 17) (RTP May 2018)

**Incorrect**

There is an inverse relationship between materiality and the degree of audit risk. The higher the materiality level, the lower the audit risk and vice versa. For example, the risk that a particular account balance or class of transactions could be misstated by an extremely large amount might be very low but the risk that it could be misstated by an extremely small amount might be very high.

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## Part B – Descriptive Questions

### ***Audit Plan to Conduct an Effective Audit***

Q. 1	<p>SA 300 state that the auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client’s business. Explain. (Refer a to d pt. only)</p> <p style="text-align: right;">(RTP May 2023)</p> <p style="text-align: center;">OR</p> <p>Plans should be made to cover acquiring knowledge of the client’s accounting systems, policies and internal control procedures. Explain.</p> <p style="text-align: center;">OR</p> <p>The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Discuss and explain what should be covered in audit plans.</p> <p style="text-align: right;">(RTP New Nov 18) (RTP Inter New Nov 19) (RTP IPCC May 19)</p> <p style="text-align: center;">OR</p> <p>“The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client’s business” Discuss stating clearly the broad points you would be covering in framing plan to conduct audit in an efficient and effective manner.</p> <p style="text-align: right;">(MTP March 2018, 5 Marks) (MTP March 2019, 4 Marks)</p> <p style="text-align: center;">OR</p> <p>Planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement. Discuss stating clearly the broad points you would be covering in framing plan to conduct audit in an efficient and effective manner.</p> <p style="text-align: right;">(MTP Oct-New 2018, 5 Marks)</p> <p style="text-align: center;">OR</p> <p>“The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner.” Explain stating the matters to be covered in plans.</p> <p style="text-align: right;">(Inter Audit MTP/ New/ Old. 2021) (4 Marks)</p>
	<p>The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client’s business.</p> <p><b>Plans should be made to cover, among other things:</b></p> <ol style="list-style-type: none"> <li>a. acquiring knowledge of the client’s accounting systems, policies and internal control procedures;</li> <li>b. establishing the expected degree of reliance to be placed on internal control;</li> <li>c. determining and programming the nature, timing, and extent of the audit procedures to be performed; and</li> <li>d. coordinating the work to be performed.</li> </ol> <p><b>Plans should be further developed and revised as necessary during the course of the audit.</b></p> <p>SA-300, “Planning an Audit of Financial Statements” further expounds this principle. According to it, planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement. Planning, however, includes consideration of the timing of certain activities and audit procedures that need to be completed prior to the performance of further audit procedures.</p> <p>The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan.</p>



## Benefits of Planning

**Q. 2** Surya and Chand Ltd is a manufacturing company engaged in the production of miscellaneous electrical goods. Trilochan and Co. has been appointed as the auditors to carry out its audit. Auditor thinks that planning an audit would involve establishing the overall audit strategy for the engagement and developing an audit plan. Also, Adequate planning benefits the audit of financial statements in several ways. Analyse and advise explaining the benefits of adequate planning.

(RTP IPCC Nov 19) (RTP New May 2018)

OR

Planning and audit involve establishing the overall audit strategy for the engagement and developing an audit plan. Adequate planning benefits the audit of financial statements in several ways. Discuss

(RTP IPCC May 18)

OR

"An adequate planning benefits the audit of financial statements." Discuss.

(5 Marks, Nov 2018 – Inter New) (4 Marks, MTP Sep.2022)

OR

Explain the benefits of planning in the audit of financial statements.

(RTP Inter New May 2019)

OR

Engagement partner of Audit Firm MKC AND COMPANY thinks that planning an audit would involve establishing the overall audit strategy for the engagement and developing an audit plan. Also, Adequate planning would benefit the audit of financial statements in several ways. Analyse explaining the benefits of adequate planning.

(RTP INTER MAY 18) (RTP IPCC MAY18) (RTP Inter New Nov 19)

OR

Planning an audit involves establishing the overall audit strategy for the engagement and developing an audit plan. Adequate planning benefits the audit of financial statements in several ways. Explain clearly those ways?

(MTP May 2023)(RTP MAY 2023)((Inter Audit RTP/ New/ Old Nov. 2021) (4 Marks)

Planning an audit involves establishing the overall audit strategy for the engagement and developing an audit plan. Adequate planning benefits the audit of financial statements in several ways, including the following:

1. Helping the auditor to devote appropriate attention to important areas of the audit.
2. Helping the auditor identify and resolve potential problems on a timely basis.
3. Helping the auditor properly organize and manage the audit engagement so that it is performed in an effective and efficient manner.
4. Assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks, and the proper assignment of work to them.
5. Facilitating the direction and supervision of engagement team members and the review of their work.
6. Assisting, where applicable, in coordination of work done by auditors of components and experts.

Examiner Comment - Few examinees wrote wrongly about the benefits of audit to the auditee organization, like for settlement of tax disputes, achieving organizational goals etc. which was not required.



## Knowledge of the Client's Business

Q. 3

In performing an audit of financial statements, the auditor should have or obtain knowledge of the business. Explain in the light of SA 315 "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment".

(RTP IPCC NOV 17) (6 Marks, May, 2005) (MTP Oct 2019, 4 Marks) (RTP IPCC Nov 12) (RTP IPCC Nov 13)

OR

'Knowledge of Client business' is one of the important principles in developing an overall audit plan. Explain.

(6 Marks, Nov 2017)

OR

Without adequate knowledge of client's business, a proper audit is not possible. It is one of the important principles in developing an overall audit plan. Explain in context with relevant SA, knowledge to be obtained by the auditor in establishing overall plan. Also explain how such an understanding would be helpful to the auditor.

(Inter Audit RTP/ New/ Old, May 2021)

OR

CA Mr. D has been appointed as an auditor of LMP Ltd. Before developing an overall audit plan, CA Mr. D wants to get an understanding and knowledge of the Client's business including applicable financial reporting framework. Guide CA D in understanding of the same with reference to the relevant Standard on Auditing?

(Inter Sugg. May 2023,4 Marks)

**Obtaining Knowledge of the business:** The auditor needs to obtain a level of knowledge of the client's business that will enable him to identify the events, transactions and practices that, in his judgment, may have significant effect on the financial information among other things.

It is one of the important principles in developing an overall audit plan. In fact, without adequate knowledge of client's business, a proper audit is not possible.

As per SA 315 – "Identifying and Assessing the Risk of Material Misstatement Through Understanding the Entity and its Environment", the auditor shall obtain an understanding of the following:

1. Relevant industry, regulatory, and other external factors including the applicable financial reporting framework.
2. The nature of the entity, including:
  - a. its operations;
  - b. its ownership and governance structures;
  - c. the types of investments that the entity is making and plans to make, including investments in special-purpose entities; and
  - d. the way that the entity is structured and how it is financed; to enable the auditor to understand the classes of transactions, account balances, and disclosures to be expected in the financial statements.
3. The entity's selection and application of accounting policies, including the reasons for changes thereto. The auditor shall evaluate whether the entity's accounting policies are appropriate for its business and consistent with the applicable financial reporting framework and accounting policies used in the relevant industry.
4. The entity's objectives and strategies, and those related business risks that may result in risks of material misstatement.
5. The measurement and review of the entity's financial performance.

In addition to the importance of knowledge of the client's business in establishing the overall audit plan, such knowledge helps the auditor to identify areas of special audit consideration, to evaluate the reasonableness both of accounting estimates and management representations, and to make judgment regarding the appropriateness of accounting policies and disclosures.

**Examiner Comment -** Many examinees misunderstood the question and mentioned the sources from where knowledge of business is to be obtained like from Memorandum of Association, Articles of Association, previous auditor's report etc. instead of writing about the knowledge of Client business being one of the Important principles in developing an overall audit plan and thereby mentioning various factors like nature of entity, relevant industry etc. Moreover, examinees did not mention specific points and wrote the answer in too general manner.



**Q. 4** Knowledge of the Client's business is one of the important principles in developing an overall audit plan. In fact, without adequate knowledge of client's business, a proper audit is not possible. As per SA-315, "Identifying and Assessing the Risk of Material Misstatement through Understanding the Entity and Its Environment", the auditor shall obtain an understanding of the relevant industry, regulatory and other external factors including the applicable financial reporting framework. Substantiate with the help of examples.

(RTP Inter New May 2020) (RTP IPCC May 2020)

As per SA-315, "Identifying and Assessing the Risk of Material Misstatement through Understanding the Entity and Its Environment", In the process of obtaining an understanding of the entity, the auditor shall obtain an understanding of the Relevant Industry, Regulatory, and Other External Factors including the applicable FRF :

**Important Examples are:**

- a. The competitive environment, including demand, capacity, product and price competition as well as cyclical or seasonal activity.
- b. Supplier and customer relationships, such as types of suppliers and customers (e.g., related parties, unified buying groups) and the related contracts with those entities.
- c. Technological developments, such as those related to the entity's products, energy supply and cost.
- d. Energy supply and cost.
- e. The effect of regulation on entity operations.

**Q. 5** Without adequate knowledge of client's business, a proper audit is not possible. The auditor shall obtain an understanding of the entity's objectives and strategies, and those related business risks that may result in risks of material misstatement. Explain giving examples.

Knowledge of the client's business is one of the important principles in developing an overall audit plan. In fact without adequate knowledge of client's business, a proper audit is not possible. As per SA-315, "Identifying and Assessing the Risk of Material Misstatement through Understanding the Entity and Its Environment", the auditor shall obtain an understanding of the entity's objectives and strategies, and those related business risks that may result in risks of material misstatement.

**Example:**

1. If one of management's objectives is to grow the business, management may develop a strategy of steady but regular growth through specific marketing campaigns and development of new markets. Alternatively, management may develop a more aggressive, complex strategy of acquiring competitors. Each of these strategies gives rise to differing business risks and potentially differing risks of material misstatement.
2. Examples of potential business risks include :
  - i. Failure to keep up to date with new products, technologies or services.
  - ii. Excessive reliance on a key supplier, product or individual, such as the owner.
  - iii. Lack of personnel with expertise to react to changes in the industry.
  - iv. Insufficient or excessive production capacity caused by inaccurate estimation of demand.
  - v. Loss of financing due to the entity's inability to meet financial covenants

## ***Establishment of Overall Audit Strategy***

**Q. 6** The establishment of the overall audit strategy and the detailed audit plan are closely inter-related. Explain

(MTP March 2019, 4 Marks)

**OR**

**"Once the overall audit strategy has been established, an audit plan can be developed to address the various matters identified in the overall audit strategy". Explain**

	<p>Once the overall audit strategy has been established, an audit plan can be developed to address the various matters identified in the overall audit strategy, taking into account the need to achieve the audit objectives through the efficient use of the auditor's resources. The establishment of the overall audit strategy and the detailed audit plan are not necessarily discrete or sequential processes, but are closely inter-related since changes in one may result in consequential changes to the other.</p>
<p><b>Q. 7</b></p>	<p><b>"Auditor shall establish an overall strategy that sets the scope, timing and directions of the audit, and that guides the development of the audit plan."</b></p> <p style="text-align: right;">(5 Marks each, May, 2011)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>Discuss the factors the auditor will consider while establishing the overall strategy.</b></p> <p style="text-align: right;">(RTP IPCC May 16)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>RGS &amp; Co. have been appointed as auditors to conduct audit of accounts of PAN Exports Ltd. for the year 2011-12. The auditors wanted to establish an overall strategy that would set the scope, timing and direction of the audit and also guide the development of the audit plan. Keeping in view the above, discuss the factors an auditor would take into consideration in establishing the overall strategy.</b></p> <p style="text-align: center;"><b>OR</b></p> <p><b>"The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan." How would you as an auditor establish the overall audit strategy?</b></p> <p style="text-align: center;"><b>OR</b></p> <p><b>Explain the factors an auditor would consider in establishing the overall audit strategy.</b></p> <p style="text-align: right;">(RTP IPCC MAY 13) (RTP IPCC MAY 17) (RTP IPCC MAY 14)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>You have been appointed as an auditor of MKP Ltd. for the first time. Discuss briefly, the factors to be considered by you while establishing overall audit strategy</b></p> <p style="text-align: right;">(Inter Audit MTP/ New/ Old. April 2022) (4 Marks)</p>
	<p><b>Establishment of Overall Strategy for Development of Audit Plan:</b> According to SA 300, "Planning an Audit of Financial Statements" the auditor shall establish an overall audit strategy that sets the scope, timing and directions of the audit, and that guides the development of the audit plan.</p> <p>In establishing the overall audit strategy, the auditor shall:</p> <ol style="list-style-type: none"> <li>Identify the characteristics of the engagement that define its scope;</li> <li>Ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required;</li> <li>Consider the factors that, in the auditor's professional judgment, are significant in directing the engagement team's efforts;</li> <li>Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed by the engagement partner for the entity is relevant; and</li> <li>Ascertain the nature, timing and extent of resources necessary to perform the engagement.</li> </ol>
<p><b>Q. 8</b></p>	<p><b>In establishing the overall audit strategy, the auditor shall identify the characteristics of the engagement that define its scope. Explain with an example.</b></p> <p style="text-align: right;">(RTP MAY 2023)</p> <p>In establishing the overall audit strategy, the auditor shall Identify the characteristics of the engagement that define its scope. For Example :</p> <ul style="list-style-type: none"> <li>▪ The expected audit coverage, including the number and locations of components to be included.</li> <li>▪ The nature of the business segments to evidence obtained be audited, including the need for specialized knowledge.</li> <li>▪ The expected use of audit in previous audits, for example, audit evidence related to risk assessment procedures and tests of controls.</li> </ul>



**Q. 9** In establishing overall audit strategy, the auditor shall ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required. Elucidate those cases by which auditor can ascertain the reporting objectives of the engagement.

(MTP May 2023)(4 Marks, Nov 2019 – Inter New)

In establishing the overall audit strategy, auditor shall ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required. The cases by which auditor can ascertain the reporting objectives of the engagement are:

1. The entity's timetable for reporting, such as at interim and final stages.
2. The organization of meetings with management and those charged with governance to discuss the nature, timing and extent of the audit work.
3. The discussion with management and those charged with governance regarding the expected type and timing of reports to be issued and other communications, both written and oral, including the auditor's report, management letters and communications to those charged with governance.
4. The discussion with management regarding the expected communications on the status of audit work throughout the engagement.

**Q. 10** The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. Discuss stating the process of establishing the overall audit strategy that would assist the auditor to determine key matters.

(RTP INTER NOV 17) (RTP Inter New Nov 18)

OR

Describe how the process of establishing the overall audit strategy assists the auditor in marshalling his human resources.

(4 Marks, May 2019 – Inter New)

OR

The engagement partner of SKC & Co., firm of Chartered Accountants appointed as auditor of Fabric India Ltd is considering as to management of key resources to be employed to conduct audit. Discuss how overall audit strategy would assist the auditor.

(MTP Oct-New 2018, 5 Marks)

OR

The engagement partner of AST AND ASSOCIATES, firm of Chartered Accountants appointed as auditor of Fabric India Ltd is considering as to management of key resources to be employed to conduct audit. Discuss how overall audit strategy would assist the auditor.

(MTP March 2018, 5 Marks)

OR

Overall audit strategy sets the scope, timing and direction of the audit, and guides the development of the more detailed audit plan. The process of establishing the overall audit strategy assists the auditor to determine such matters as for example - the resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas or the involvement of experts on complex matters. Explain the other three such matters.

(RTP Inter New May 2020) (RTP IPCC May 2020)

The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan.

The process of establishing the overall audit strategy assists the auditor to determine, subject to the completion of the auditor's risk assessment procedures, such matters as:

1. The resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas or the involvement of experts on complex matters;

	<ol style="list-style-type: none"> <li>2. The amount of resources to allocate to specific audit areas, such as the number of team members assigned to observe the inventory count at material locations, the extent of review of other auditors' work in the case of group audits, or the audit budget in hours to allocate to high risk areas;</li> <li>3. When these resources are to be deployed, such as whether at an interim audit stage or at key cut-off dates; and</li> <li>4. How such resources are managed, directed and supervised, such as when team briefing and debriefing meetings are expected to be held, how engagement partner and manager reviews are expected to take place (<b>for example, on-site or off-site</b>), and whether to complete engagement quality control reviews.</li> </ol>
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## Developing the Audit Plan

Q. 11	<p><b>Engagement Partner CA Hitesh Kapur of Kapur and Associates wanted to develop an audit plan of Sampurna Fabrics Ltd. Discuss the matters to be described in such an audit plan.</b></p> <p style="text-align: right;">(Inter Audit RTP/ New/ Old May. 2022 (4 Marks))</p> <p>The auditor shall develop an audit plan that shall include a description of.</p> <ol style="list-style-type: none"> <li>1) The nature, timing and extent of planned risk assessment procedures, as determined under SA 315 "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment".</li> <li>2) further The nature, timing and extent of planned further audit procedures at the assertion level, as determined under SA 330 "The Auditor's Responses to Assessed Risks".</li> <li>3) Other planned audit procedures that are required to be carried out so that the engagement complies with SAs</li> </ol> <p>The audit plan is more detailed than the overall audit strategy that includes the nature, timing and extent of audit procedures to be performed by engagement team members. Planning for these audit procedures takes place over the course of the audit as the audit plan for the engagement develops.</p> <p><b>Example</b></p> <p>Planning of the auditor's risk assessment procedures occurs early in the audit process.</p> <p>However, planning the nature, timing and extent of specific further audit procedures depends on the outcome of those risk assessment procedures. In addition, the auditor may begin the execution of further audit procedures for some classes of transactions, account balances and disclosures before planning all remaining audit procedures</p>
Q. 12	<p><b>Elucidate the matters to be considered by an auditor in developing his overall plan for the expected scope and conduct of audit.</b></p> <p style="text-align: right;">(4 MARKS, MAY 2019)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>M &amp; Co. was appointed as auditor of IGI Ltd. As an auditor what are the factors that would be considered in the development of overall audit plan?</b></p> <p style="text-align: right;">(MTP APRIL 2019, 4 MARKS) (5 MARKS, MAY 2018 - INTER NEW)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>Your firm has been appointed as an auditor to audit the accounts of an auto parts manufacturer, ABC LTD. Elucidate the matters to be considered by an auditor in developing his overall plan for the expected scope and conduct of audit.</b></p> <p style="text-align: right;">(MTP OCT 2020, 4 MARKS)</p> <p><b>Development of an Overall Plan:</b> The auditor should consider the following matters in developing his overall plan for the expected scope and conduct of the audit-</p> <ul style="list-style-type: none"> <li>▪ The terms of his engagement and any statutory responsibilities.</li> <li>▪ The nature and timing of reports or other communication.</li> <li>▪ The applicable legal or statutory requirements.</li> <li>▪ The accounting policies adopted by the client and changes in those policies.</li> </ul>

- The effect of new accounting or auditing pronouncements on the audit.
- The identification of significant audit areas.
- The setting of materiality levels for audit purposes.
- Conditions requiring special attention, such as the possibility of material error or fraud or the involvement of parties in whom directors or persons who are substantial owners of the entity are interested and with whom transactions are likely.
- The degree of reliance he expects to be able to place on accounting system and internal control.
- Possible rotation of emphasis on specific audit areas.
- The nature and extent of audit evidence to be obtained.
- The work of internal auditors and the extent of their involvement, if any, in the audit.
- The involvement of other auditors in the audit of subsidiaries or branches of the client.
- The involvement of experts.
- The allocation of work to be undertaken between joint auditors and the procedures for its control and review.
- Establishing and coordinating staffing requirements.

**Examiner Comment -** Examinees could cover only few correct points and some of them mixed the points with principle aspects required to be looked into by the auditor instead of development of plan.

## ***Audit Planning – A Continuous Process***

**Q. 13** "Planning is not a discrete phase of an audit, but rather a continual and iterative process." Discuss.  
(5 MARKS, NOV 2018 – INTER NEW)

OR

**Planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after the completion of the previous audit and continues until the completion of the current audit engagement. Analyse and Explain.**

(RTP INTER NEW NOV 19)

OR

**Plans should be further developed and revised as necessary during the course of the audit. Explain.**

(RTP INTER NEW MAY 2020) (RTP IPCC MAY 2020)

Or

**Planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after the completion of the previous audit and continues until the completion of the current audit engagement. Planning includes the need to consider certain matters prior to the auditor's identification and assessment of the risks of material misstatement. Explain clearly stating those matters also.**

(Inter Audit RTP/ New/ Old, May, 2021)

### **Audit Planning- a Continuous Process**

Planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement. Planning, however, includes consideration of the timing of certain activities and audit procedures that need to be completed prior to the performance of further audit procedures. For example, planning includes the need to consider, prior to the auditor's identification and assessment of the risks of material misstatement, such matters as:

1. The analytical procedures to be applied as risk assessment procedures.
2. Obtaining a general understanding of the legal and regulatory framework applicable to the entity and how the entity is complying with that framework.
3. The determination of materiality.

4. The involvement of experts.
5. The performance of other risk assessment procedures.

Examiner Comment - Examinees could not understand the question and mentioned either the benefits of planning or simply focused as audit planning is a continuous process. They did not explain fields where the audit planning as a continuous process is required.

### **Updating and Changing the Strategy and Audit Plan**

**Q. 14** The auditor shall update and change the overall audit strategy and the audit plan as necessary during the course of the audit. Explain

OR

**As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan. Explain.**

(MTP AUG-NEW 2018, 5 MARKS) (RTP INTER NEW NOV 18) (RTP INTER NOV 17) (RTP INTER NEW NOV 19)

- **The auditor shall update and change the overall audit strategy** and the audit plan as necessary during the course of the audit. As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan and thereby the resulting planned nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks.
- This may be the case when information comes to the auditor's attention that differs significantly from the information available when the auditor planned the audit procedures.  
**For example, audit** evidence obtained through the performance of substantive procedures may contradict the audit evidence obtained through tests of controls.

### **Direction, Supervision & Review [Para 10, A.15]**

**Q. 15** The auditor shall plan the nature, timing and extent of direction and supervision of engagement team members and the review of their work. Explain the factors due to which above varies.

(MTP MAY 2020, 4 MARKS)

Or

**The nature, timing and extent of the direction and supervision of engagement team members and review of their work vary depending on many factors. Explain those factors.**

(Inter RTP Nov. 2022)

Or

**The auditor shall plan the nature, timing and extent of direction and supervision of engagement team members and the review of their work. The nature, timing and extent of the direction and supervision of engagement team members and review of their work vary depending on many factors. Explain giving eg.**

Or

**" The nature, timing and extent of the direction and supervision of engagement team members and review of their work vary depending on many factors." Explain**

The auditor shall plan the nature, timing and extent of direction and supervision of engagement team members and the review of their work.

The nature, timing and extent of the direction and supervision of engagement team members and review of their work vary depending on many factors, including:

1. The size and complexity of the entity.
2. The area of the audit.



3. The assessed risks of material misstatement
4. The capabilities and competence of the individual team members performing the audit work.

**Example :**An increase in the assessed risk of material misstatement for a given area of the audit ordinarily requires a corresponding increase in the extent and timeliness of direction and supervision of engagement team members, and a more detailed review of their work.

**Example :** We may have identified a problem related to the production process that raised concerns about inventory obsolescence. After obtaining an understanding of the entity's process that raised concerns about inventory obsolescence (which we had identified as a significant class of transactions), we concluded that additional tests of details were required. Therefore, the senior will likely take part, along with the team, in the discussions with management about the provision for obsolescence and examine related documentation supporting the provision, rather than just reading the memo on file. These procedures should be completed as the work is being performed rather than as an after the fact review. The extent of the senior's involvement requires judgment, taking into consideration the complexity of the area and the experience of the team.

## Documentation

**Q. 16** The auditor shall document the overall audit strategy, the audit plan and any significant changes made during the audit engagement to the overall audit strategy or the audit plan, and the reasons for such changes. Explain

(MTP AUG-NEW 2018, 5 MARKS) (RTP INTER NEW NOV 18) (RTP INTER NOV 17)

Or

The auditor shall document the overall audit strategy, the audit plan and any significant changes made to the overall audit strategy or the audit plan. Explain in detail giving examples.

[MTP-Aug. 18, RTP-Nov. 18, Nov. 20]

Or

Is it necessary to document the audit plan? If so, what all activities in the planning phase needs to be documented? State with Examples?

(TYK)

The auditor shall document:

- a. the overall audit strategy;
- b. the audit plan; and
- c. any significant changes made during the audit engagement to the overall audit strategy or the audit plan, and the reasons for such changes.

The documentation of the overall audit strategy is a record of the key decisions considered necessary to properly plan the audit and to communicate significant matters to the engagement team.

**For example,** the auditor may summarize the overall audit strategy in the form of a memorandum that contains key decisions regarding the overall scope, timing and conduct of the audit.

The documentation of the audit plan is a record of the planned nature, timing and extent of risk assessment procedures and further audit procedures at the assertion level in response to the assessed risks. It also serves as a record of the proper planning of the audit procedures that can be reviewed and approved prior to their performance. The auditor may use standard audit programs and/or audit completion checklists, tailored as needed to reflect the particular engagement circumstances.

A record of the significant changes to the overall audit strategy and the audit plan, and resulting changes to the planned nature, timing and extent of audit procedures, explains why the significant changes were made, and the overall strategy and audit plan finally adopted for the audit. It also reflects the appropriate response to the significant changes occurring during the audit.

**For instance-**

**The following things should form part of auditor's documentation:**





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	<ul style="list-style-type: none"> <li>▪ A summary of discussions with the entity's key decision makers</li> <li>▪ Documentation of audit committee pre-approval of services, where required</li> <li>▪ Audit documentation access letters</li> <li>▪ Other communications or agreements with management or those charged with governance regarding the scope, or changes in scope, of our services</li> <li>▪ auditor's report on the entity's financial statements.</li> <li>▪ Other reports as specified in the engagement agreement (e.g., debt covenant compliance letter)</li> </ul>
<b>Q. 17</b>	<p><b>Explain what do you mean by documentation of audit plan. Discuss the purpose served by it and also elaborate the tools used by the auditor to reflect the particular engagement circumstances.</b></p> <p style="text-align: right;">(Inter RTP Nov 2022)</p> <p>The documentation of the audit plan is a record of the planned nature, timing and extent of risk assessment procedures and further audit procedures at the assertion level in response to the assessed risks. It also serves as a record of the proper planning of the audit procedures that can be reviewed and approved prior to their performance.</p> <p>The auditor may use standard audit programs and/or audit completion checklists, tailored as needed to reflect the particular engagement circumstances.</p>

## Audit Programme

<b>Q. 18</b>	<p><b>Write a short note on - Audit Programme.</b></p> <p style="text-align: right;">(4 MARKS, NOVEMBER, 2006)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>"An audit programme is a detailed plan of applying the audit procedure in the given circumstance for accomplishing the audit objectives". Discuss.</b></p> <p style="text-align: right;">(RTP IPCC MAY 16)</p>
	<p><b>Audit Programme :</b> An audit programme consists of a series of verification procedures to be applied to the financial statements and accounts of a given company for the purpose of obtaining sufficient evidence to enable the auditor to express an informed opinion on such statements.</p> <p><b>In other words,</b></p> <p>An audit programme is a detailed plan of applying the audit procedure in the given circumstances with instructions for the appropriate techniques to be adopted for accomplishing the audit objectives.</p> <p>To start with, an auditor having regard to the nature, size and composition of the business and the dependability of the internal control and the given scope of work, should frame a programme which should aim at providing for a minimum essential work which may be termed as a standard programme.</p> <p>As experience is gained by actually carrying out the work, the programme may be altered to take care of situations which were left out originally, but are found relevant for the particular concern.</p> <p>Similarly, if any work originally provided for proves beyond doubt to be unnecessary or irrelevant, it may be dropped.</p> <p>There should be periodic review of the audit programme to assess whether the same continues to be adequate for obtaining requisite knowledge and evidence about the transactions.</p>
<b>Q. 19</b>	<p><b>a. Evolving one audit programmed applicable to all business under all circumstances is not practicable. Explain clearly stating in detail the meaning of audit programme.</b></p> <p><b>b. In most of the assertions much of the evidence be drawn and each one should be considered and weighed to ascertain its weight to prove or disprove the assertion. An auditor picks up evidence from a variety of fields. Analyse and explain with the help of examples.</b></p> <p style="text-align: right;">(RTP Nov 20)</p>
	<p><b>a.</b> Businesses vary in nature, size and composition; work which is suitable to one business may not be suitable to others; efficiency and operation of internal controls and the exact nature of the service to be rendered by the auditor are the other factors that vary from assignment to assignment. On account of such variations, evolving one audit programmed applicable to all business under all circumstances is not practicable.</p>



However, it becomes a necessity to specify in detail in the audit programmed the nature of work to be done so that no time will be wasted on matters not pertinent to the engagement and any special matter or any specific situation can be taken care of.

It is desirable that in respect of each audit and more particularly for bigger audits an audit programmed should be drawn up. Audit programmed is a list of examination and verification steps to be applied and set out in such a way that the inter-relationship of one step to another is clearly shown and designed, keeping in view the assertions discernible in the statements of account produced for audit or on the basis of an appraisal of the accounting records of the client.

**Definition:** An audit programmed consists of a series of verification procedures to be applied to the financial statements and accounts of a given company for the purpose of obtaining sufficient evidence to enable the auditor to express an informed opinion on such statements.

In other words, an audit programmed is a detailed plan of applying the audit procedures in the given circumstances with instructions for the appropriate techniques to be adopted for accomplishing the audit objectives.

- b. In most of the assertions much of the evidence be drawn and each one should be considered and weighed to ascertain its weight to prove or disprove the assertion. In this process, an auditor would be in a position to identify the evidence that brings the highest satisfaction to him about the appropriateness or otherwise of the assertion.

**An auditor picks up evidence from a variety of fields and it is generally of the following broad types:**

1. Documentary examination,
2. Physical examination,
3. Statements and explanation of management, officials and employees,
4. Statements and explanations of third parties,
5. Arithmetical calculations by the auditor,
6. State of internal controls and internal checks,
7. Inter-relationship of the various accounting data,
8. Subsidiary and memorandum records,
9. Minutes,
10. Subsequent action by the client and by others.

**Example**

1. For cash in hand, the best evidence is 'count'
2. For investment pledged with a bank, the banker's certificate.
3. For verifying assertions about book debts, the client's ledger invoices, debit notes, credit notes, monthly accounts statement sent to the customers are all evidence: some of these are corroborative, other being complementary. In addition, balance confirmation procedure is often resorted to, to obtain greater satisfaction about the reliability of the assertion.

The auditor, however, has to place appropriate weight on each piece of evidence and accordingly should prescribe the priority of verification. It is true that in all cases one procedure may not bring the highest satisfaction and it may be dangerous for the auditor to ignore any evidence that is available. By the word "available" we do not mean that the evidence available with the client is the only available evidence. The auditor should know what normally should be available in the context of the transaction having regard to the circumstances and usage.

## ***Evolving One Audit Programme***

**Q. 20 Evolving one audit programme applicable to all audit engagements under all circumstances is not practicable. Explain.**

(RTP INTER MAY 18) (RTP IPCC MAY 18) (RTP INTER NEW MAY 19)

**Businesses vary in nature, size and composition;** work which is suitable to one business may not be suitable to others; efficiency and operation of internal controls and the exact nature of the service to be rendered by the auditor are the other factors that vary from assignment to assignment. On account of such variations, evolving one audit programme applicable to all businesses under all circumstances is not practicable. However, it becomes a necessity to specify in detail in the audit programme the nature of work to be done so that no time will be wasted on matters not pertinent to the engagement and any special matter or any specific situation can be taken care of.

<b>Q. 21</b>	<p><b>M/s TP &amp; Co., a firm of Chartered Accountants, is auditor of KSR Ltd. for many years. KSR Ltd. has diversified their business into newer areas during the last year. The senior member of the audit team handed over the standard audit programme of earlier years to the audit assistants and instructed them to follow the same. The assistants are conducting the audit accordingly. Whether the attitude of the audit assistants is justified or they are required to keep an open mind? Guide them.</b></p>
	<p><b>The Assistant Engaged – Be Encouraged to Keep an Open Mind:</b></p> <p>To start with, an auditor having regard to the nature, size and composition of the business and the dependability of the internal control and the given scope of work, should frame a programme which should aim at providing for a minimum essential work which may be termed as a standard programme.</p> <p>As experience is gained by actually carrying out the work, the programme may be altered to take care of situations which were left out originally, but are found relevant for the particular concern. Similarly, if any work originally provided for proves beyond doubt to be unnecessary or irrelevant, it may be dropped. The assistant engaged in the job should be encouraged to keep an open mind beyond the programme given to him.</p> <p>He should be instructed to note and report significant matters coming to his notice, to his seniors or to the partners or proprietor of the firm engaged for doing the audit. In the given case, the attitude of assistants of TP &amp; Co. is not justified. They should keep an open mind and go beyond the programme to take care of newer areas of the business of KSR Ltd. into which the Company has diversified.</p>

### **Periodic Review of The Audit Programme**

<b>Q. 22</b>	<p><b>The utility of the audit programme can be retained and enhanced only by keeping the programme as also the client's operations and internal control under periodic review so that inadequacies or redundancies of the programme may be removed. Explain</b></p> <p style="text-align: right;">(RTP INTER NEW MAY 19)</p>
	<p><b>Periodic Review of The Audit Programme</b></p> <ul style="list-style-type: none"> <li>▪ There should be periodic review of the audit programme to assess whether the same continues to be adequate for obtaining requisite knowledge and evidence about the transactions. Unless this is done, any change in the business policy of the client may not be adequately known, and consequently, audit work may be carried on, on the basis of an obsolete programme and, for this negligence, the whole audit may be held as negligently conducted and the auditor may have to face legal consequences.</li> <li>▪ <b>Example-</b> If the audit programme for the audit of a branch of a financing house, drawn up a number of years ago, fails to take into consideration that the previous policy of financing of a vehicle has been changed to financing of real estate acquisition, the whole audit conducted thereunder would be entirely misdirected and may even result into nothing more than a farce. [Pacific Acceptance Corporation Ltd. v. Forsyth and Others.]</li> <li>▪ The utility of the audit programme can be retained and enhanced only by keeping the programme as also the client's operations and internal control under periodic review so that inadequacies or redundancies of the programme may be removed. However, as a basic feature, audit programme not only lists the tasks to be carried out but also contains a few relevant instructions, like the extent of checking, the sampling plan, etc.</li> <li>▪ So long as the programme is not officially changed by the principal, every assistant deputed on the job should unflinchingly carry out the detailed work according to the instructions governing the work. Many persons believe that this brings an element of rigidity in the audit programme.</li> <li>▪ This is not true provided the periodic review is undertaken to keep the programme as up-to-date as possible and by encouraging the assistants on the job to observe all salient features of the various accounting functions of the client.</li> </ul>
<b>Q. 23</b>	<p><b>"The utility of the audit programme can be retained and enhanced only by keeping the programme and also the client's operations and internal control under periodic review so that inadequacies or redundancies of the programme may be removed". Discuss stating clearly the advantages of an audit programme.</b></p>
	<p>The utility of the audit programme can be retained and enhanced only by keeping the programme as also the client's operations and internal control under periodic review so that inadequacies or redundancies of the programme may be removed. However, as a basic feature, audit programme not only lists the tasks to be carried out but also contains a few relevant instructions, like the extent of checking, the sampling plan, etc.</p>



So long as the programme is not officially changed by the principal, every assistant deputed on the job should unfailingly carry out the detailed work according to the instructions governing the work. Many persons believe that this brings an element of rigidity in the audit programme.

Refer Qn27 for advantages.

## ***Constructing an Audit Programme***

**Q. 24** What is an audit programme ? Discuss the points you should keep in mind for the purpose of programme construction.

(RTP IPCC MAY 14)

OR

List out the points that should be kept in mind by the auditor for the purpose of constructing an audit programme.

(3 Marks, May 2019 – Inter New)

OR

Arpana Hospitals Ltd having Gross Professional Charges of ` 50 crores is engaged in providing healthcare services. STP & Co., a firm of auditors is appointed as its auditors.

Advise what special points to be kept in mind for the purpose of construction of an Audit programme. Explain.

OR

State what special points you would keep in mind for the purpose of construction of an Audit programme. Explain.

(RTP INTER MAY 18) (RTP IPCC MAY 18)

OR

Discuss the points to be considered by auditor for the purpose of constructing an audit programme.

(4 Marks, Nov 2019 – Inter New)

OR

XYZ & associates are appointed as the statutory auditors of Fisco Ltd. for the FY 2021-22. While constructing the audit programme, the engagement partner, CA X, should keep in mind various points. List such points.

(4 Marks, MTP Oct.2022)

An audit programme consists of a series of verification procedures to be applied to the financial statements and accounts of a given company for the purpose of obtaining sufficient evidence to enable the auditor to express an informed opinion on such statements.

For the purpose of programme construction, the following points should be kept in view:

1. Stay within the scope and limitation of the assignment.
2. Prepare a written audit programme setting forth the procedures that are needed to implement the audit plan.
3. Determine the evidence reasonably available and identify the best evidence for deriving the necessary satisfaction.
4. Apply only those steps and procedures which are useful in accomplishing the verification purpose in the specific situation.
5. Include the audit objectives for each area and sufficient details which serve as a set of instructions for the assistants involved in audit and help in controlling the proper execution of the work.
6. Consider all possibilities of error.
7. Co-ordinate the procedures to be applied to related items.

<b>Q. 25</b>	<p><b>While developing an audit programme, the auditor may conclude that relying on certain internal controls is an effective and efficient way to conduct his audit. Explain stating clearly the points to be kept in mind while developing an audit programme.</b></p> <p style="text-align: right;">(Inter RTP Nov. 2022)</p>
	<p>While developing an audit programme, the auditor may conclude that relying on certain internal controls is an effective and efficient way to conduct his audit. However, the auditor may decide not to rely on internal controls when there are other more efficient ways of obtaining sufficient appropriate audit evidence. The auditor should also consider the timing of the procedures, the coordination of any assistance expected from the client, the availability of assistants, and the involvement of other auditors or experts.</p> <p>For the purpose of programme construction, the following points should be kept in mind: <b>Refer Above Q.24</b></p>

### ***Audit Programme- Designed to provide Audit Evidence***

<b>Q. 26</b>	<p><b>Evidence is the very basis for formulation of opinion and an audit programme is designed to provide for that by prescribing procedures and techniques.</b></p> <p><b>Analyse and explain with the help of example of evidence in respect of Sales</b></p> <p style="text-align: right;">(RTP Inter New May 2020) (RTP IPCC May 2020)</p>
	<p>Evidence is the very basis for formulation of opinion and an audit programme is designed to provide for that by prescribing procedures and techniques.</p> <p>What is best evidence for testing the accuracy of any assertion is a matter of expert knowledge and experience.</p> <p>This is the primary task before the auditor when he draws up the audit programme. Transactions are varied in nature and impact; procedures to be prescribed depend on prior knowledge of what evidence is reasonably available in respect of each transaction.</p> <p><b>Example :</b></p> <p><b>Sales are evidenced by:</b></p> <ol style="list-style-type: none"> <li>i. invoices raised by the client;</li> <li>ii. price list;</li> <li>iii. forwarding notes to client;</li> <li>iv. inventory-issue records;</li> <li>v. sales managers' advice to the inventory section;</li> <li>vi. acknowledgements of the receipt of goods by the customers; and</li> <li>vii. collection of money against sales by the client.</li> </ol>

### ***Developing the Audit Programme***

<b>Q. 27</b>	<p><b>Explain the significant points auditor would consider while developing an audit programme.</b></p> <p style="text-align: right;">(RTP Inter New May 19)</p>
	<p><b>Developing the Audit Programme :</b></p> <ol style="list-style-type: none"> <li><b>1. Written Audit Programme :</b> The auditor should prepare a written audit programme setting forth the procedures that are needed to implement the audit plan.</li> <li><b>2. Audit objective and instruction to assistants :</b> The programme may also contain the audit objectives for each area and should have sufficient details to serve as a set of instructions to the assistants involved in the audit and as a means to control the proper execution of the work.</li> </ol>



3. **Reliance on Internal Controls :** In preparing the audit programme, the auditor, having an understanding of the accounting system and related internal controls, may wish to rely on certain internal controls in determining the nature, timing and extent of required auditing procedures. The auditor may conclude that relying on certain internal controls is an effective and efficient way to conduct his audit. However, the auditor may decide not to rely on internal controls when there are other more efficient ways of obtaining sufficient appropriate audit evidence. The auditor should also consider the timing of the procedures, the coordination of any assistance expected from the client, the availability of assistants, and the involvement of other auditors or experts.
4. **Timings of performance of audit procedures :** The auditor normally has flexibility in deciding when to perform audit procedures. However, in some cases, the auditor may have no discretion as to timing, for example, when observing the taking of inventories by client personnel or verifying the securities and cash balances at the year-end.
5. **Audit planning:** The audit planning ideally commences at the conclusion of the previous year's audit, and along with the related programme, it should be reconsidered for modification as the audit progresses. Such consideration is based on the auditor's review of the internal control, his preliminary evaluation thereof, and the results of his compliance and substantive procedures.

## **Advantages and Disadvantages of an Audit Programme**

- Q. 28** "All the disadvantages of audit program may be eliminated by imaginative supervision of the work carried on by the assistants." Explain stating the advantages and disadvantages of an audit program.  
(RTP IPCC MAY 17) (RTP IPCC NOV15) (PM IPCC CH4) (4 MARKS, May, 2012)
- OR**
- State the disadvantages of the use of an Audit programme.**  
(4 Marks, Nov 2018)
- OR**
- "All the disadvantages of audit program may be eliminated by imaginative supervision of the work carried on by the assistants, the auditor must have a receptive attitude as regards the assistants; the assistants should be encouraged to observe matters objectively and bring significant matters to the notice of supervisor/principal." Explain stating the advantages and disadvantages of an audit program.  
(RTP IPCC Nov 19)
- OR**
- Disadvantages of the use of an audit programme.**  
(MTP Aug 2018, 4 Marks) (RTP IPCC Nov 15)
- OR**
- CA Vikas Jain discussed with his audit team about advantages and disadvantages of audit programme. He explained to his team that – "work may become mechanical" as disadvantage of the audit programme. Discuss explaining the disadvantages of an audit programme.**  
(Inter Audit MTP/ New/ Old. May 2022) (4 Marks)

### **Advantages and Disadvantages of the use of an Audit Programme**

**The advantages of an audit programme are:**

1. It provides the assistant carrying out the audit with total and clear set of instructions of the work generally to be done.
2. It is essential, particularly for major audits, to provide a total perspective of the work to be performed.
3. Selection of assistants for the jobs on the basis of capability becomes easier when the work is rationally planned, defined and segregated.
4. Without a written and pre-determined programme, work is necessarily to be carried out on the basis of some 'mental' plan. In such a situation there is always a danger of ignoring or overlooking certain books and records. Under a properly framed programme, the danger is significantly less and the audit can proceed systematically.
5. The assistants, by putting their signature on programme, accept the responsibility for the work carried out by them individually and, if necessary, the work done may be traced back to the assistant.



	<p>6. The principal can control the progress of the various audits in hand by examination of audit programmes initiated by the assistants deputed to the jobs for completed work.</p> <p>7. It serves as a guide for audits to be carried out in the succeeding year.</p> <p>8. A properly drawn up audit programme serves as evidence in the event of any charge of negligence being brought against the auditor. It may be of considerable value in establishing that he exercised reasonable skill and care that was expected of professional auditor.</p> <p><b>Some disadvantages are also there in the use of audit programmes, but most of these can be removed by taking some concrete steps. The disadvantages are:</b></p> <ol style="list-style-type: none"> <li>1. The work may become mechanical and particular parts of the programme may be carried out without any understanding of the object of such parts in the whole audit scheme.</li> <li>2. The programme often tends to become rigid and inflexible following set grooves; the business may change in its operation of conduct, but the old programme may still be carried on. Changes in staff or internal control may render precaution necessary at points different from those originally decided upon.</li> <li>3. Inefficient assistants may take shelter behind the programme i.e. defend deficiencies in their work on the ground that no instruction in the matter is contained therein. A hard and fast audit programme may kill the initiative of efficient and enterprising assistants.</li> <li>4. All these disadvantages may be eliminated by imaginative supervision of the work carried on by the assistants; the auditor must have a receptive attitude as regards the assistants; the assistants should be encouraged to observe matters objectively and bring significant matters to the notice of supervisor/principal.</li> </ol>
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### **Audit Planning and Materiality (SA 320) – Qn 29 to 33**

<b>Q. 29</b>	<p><b>Discuss the concept of materiality in the context of the preparation and presentation of financial statements.</b></p> <p style="text-align: right;">(RTP IPCC Nov 17) (RTP IPCC MAY 13) (RTP IPCC NOV 17) (RTP IPCC NOV 18)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>Financial reporting frameworks often discuss the concept of materiality in the context of the preparation and presentation of financial statements. Explain</b></p> <p style="text-align: right;">(RTP May 2021)</p>
	<p>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:</p> <ol style="list-style-type: none"> <li>1) Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements;</li> <li>2) Judgments about materiality are made in the light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both; and</li> <li>3) 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. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered.</li> </ol>
<b>Q. 30</b>	<p><b>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, explain the auditor's assumptions about users of the financial statements.</b></p> <p style="text-align: right;">(RTP May 2021)</p>
	<p>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:</p>

	<ol style="list-style-type: none"> <li>1. 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;</li> <li>2. Understand that financial statements are prepared, presented and audited to levels of materiality; Recognize</li> <li>3. the uncertainties inherent in the measurement of amounts based on the use of estimates, judgment and the consideration of future events; and</li> <li>4. Make reasonable economic decisions on the basis of the information in the financial statements.</li> </ol>
<b>Q. 31</b>	<p><b>Explain the concept of “Materiality” as discussed in SA 320.</b></p> <p style="text-align: right;">(RTP Old May 13)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>Explain concept of ‘Materiality’.</b></p> <p style="text-align: right;">(RTP Old May 16) (RTP IPCC MAY 16) (RTP IPCC Nov 18)</p>
	<p><b>Concept of Materiality:</b> As per SA 320 “Materiality in Planning and Performing an Audit”, 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:</p> <p><b>REFER Q29 Pt. 1 -3</b></p> <p>Such a discussion, if present in the applicable financial reporting framework, provides a frame of reference to the auditor in determining materiality for the audit. If the applicable financial reporting framework does not include a discussion of the concept of materiality, the characteristics referred above provides the auditor with such a frame of reference.</p> <p>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, <b>it is reasonable for the auditor to assume that users :</b></p> <p><b>REFER Q30. Pt. 1-4</b></p> <p>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>
<b>Q. 32</b>	<p><b>A senior assistant of A &amp; Co. Chartered Accountants detected a mistake of ` 7 per interest payment which have recurred number of times. General Manager (Finance) of R Ltd. suggested him not to request for passing any adjustment entry as individually the errors were of small amounts. The company had 1,500 deposit accounts and interest was paid quarterly.</b></p> <p style="text-align: right;">(RTP Old Nov 11) (RTP IPCC NOV 11)</p>
	<p><b>Responsibility of Auditor while detection of mistake :</b> Materiality has been defined by SA 320 “Materiality in Planning and Performing an Audit” as Misstatements, including omissions, if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.</p> <p>In the situation given the error, apparently, seems to be of small amount (Rs 7) and General Manager (Finance) is of the opinion that it is , therefore, not material and thus there is no need to pass any adjustment entry.</p> <p>The audit assistant should not accept the argument of the General Manager because there are 1500 deposit accounts and interest payment is quarterly. If the cumulative effect of these small amounts is considered, as per the requirements of SA 320 error of Rs. 7 which has recurred a number of times may become material. If considered “immaterial” it may cause an overstatement of income. Hence, the auditor should apply expanded substantive procedures to assess the cumulative effect of these small amounts.</p>
<b>Q. 33</b>	<p><b>What could be considered material for all situations cannot be defined precisely and an amount or transaction material in one situation may not be material in other situation. Explain?</b></p> <p style="text-align: right;">(Old Course SM) (Inter Audit RTP/ New/ Old Nov. 2021 (4 Marks)</p> <p>Materiality is an important consideration for an auditor to evaluate whether the financial statements reflect a true and fair view or not. SA 320 on “Materiality in Planning and Performing an Audit” requires that an auditor should consider materiality and its relationship with audit risk while conducting an audit.</p> <p>When planning the audit, the auditor considers what would make the financial information materially misstated.</p>

	<p>The auditor's preliminary assessment of materiality related to specific account balances and classes of transactions helps the auditor decide such questions as what items to examine and whether to use sampling and analytical procedures. This enables the auditor to select audit procedures that, in combination, can be expected to support the audit opinion at an acceptably low degree of audit risk.</p> <p>It may be noted that the auditor's assessment of materiality and audit risk may be different at the time of initially planning of the audit as against at the time of evaluating the results of audit procedures.</p> <p>At the planning stage, the auditor needs to consider the materiality for the financial statements as a whole. The auditor has to carry out a preliminary identification of significant components and material classes of transactions, account balances and disclosure which he plans to examine.</p> <p>What could be considered material for all situations cannot be defined precisely and an amount or transaction material in one situation may not be material in other situation. For example, ` 5,000 may be material for a small entity, but even ` 100,000 may not be material for a large entity.</p>
<p><b>Q. 34</b></p>	<p><b>Whether misstatements of lesser amounts than 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? Explain with examples.</b></p> <p style="text-align: right;">(TYK)</p>
	<p>When establishing the overall audit strategy, the auditor shall determine materiality for the financial statements as a whole. If, in the specific circumstances of the entity, there is one or more particular classes of transactions, account balances or disclosures 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 classes of transactions, account balances or disclosures</p>

## Benchmarking

<p><b>Q. 35</b></p>	<p><b>With reference to SA 320 "Materiality in planning and performing an audit", indicate the factors which may affect the identification of an appropriate bench mark in determining materiality for the financial statement as a whole.</b></p> <p style="text-align: right;">(RTP IPCC May 19) (5 Marks, Nov 2015) (Audit / Nov. 2020) (4 Marks)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>"Determining materiality involves the exercise of professional judgment". Discuss stating the factors that may affect the identification of an appropriate benchmark. Also give example</b></p> <p style="text-align: center;"><b>OR</b></p> <p><b>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. Discuss stating the factors that may affect the identification of an appropriate benchmark</b></p> <p style="text-align: right;">(RTP INTER MAY 18) (RTP IPCC MAY18)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>You are being appointed as the auditor of Track Ltd. for the first time. You want to determine the materiality level and for that you have applied percentage to choose benchmark as a starting point in determining materiality for the financial statements as a whole. What are the factors that may affect the identification of an appropriate benchmark?</b></p> <p style="text-align: right;">((Inter Audit RTP/ New/ Old May. 2022 (4 Marks)</p> <p style="text-align: right;">OR</p> <p><b>An auditor has to exercise professional judgement in determining materiality. Explain the factors that may affect the identification of an appropriate benchmark in determining materiality for the financial statements as whole.</b></p> <p style="text-align: right;">(Inter Audit Suggested / New May. 2023)</p>
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Factors that may affect the Identification of an Appropriate Benchmark in Determining Materiality:

As per SA 320 "Materiality in Planning and Performing an Audit", 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-

- i. The elements of the financial statements (for example, assets, liabilities, equity, revenue, expenses);
- ii. 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);
- iii. 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;
- iv. 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
- v. The relative volatility of the benchmark.

Examiner Comment - Many examinees discussed about materiality instead of explaining about the factors which may affect identification of an appropriate benchmark in determining materiality for the financial statement as a whole.

### **Revision in Materiality level as the Audit Progresses**

**Q. 36** As an auditor of RST Ltd. Mr. P applied the concept of materiality for the financial statements as a whole. On the basis of obtaining additional information of significant contractual arrangements that draw attention to a particular aspect of a company's business, he wants to re-evaluate the materiality concept. Please guide him.

OR

**Materiality for the financial statements as a whole may need to be revised as a result of a change in circumstances that occurred during the audit. Explain with the help of example.**

(MTP Oct 2019, 3 Marks)

- **Revision in Materiality level as the Audit Progresses:** Materiality for the financial statements as a whole (and, if applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures) may need to be revised as a result of a change in circumstances that occurred during the audit (for example, a decision to dispose of a major part of the entity's business), new information, or a change in the auditor's understanding of the entity and its operations as a result of performing further audit procedures.
- If the auditor concludes that a lower materiality for the financial statements as a whole (and, if applicable, materiality level or levels for particular classes of transactions, account balances or disclosures) than that initially determined is appropriate, the auditor shall determine whether it is necessary to revise performance materiality, and whether the nature, timing and extent of the further audit procedures remain appropriate.
- **Example:** If during the audit it appears as though actual financial results are likely to be substantially different from the anticipated period end financial results that were used initially to determine materiality for the financial statements as a whole, the auditor revises that materiality.

### **Standard's**

**Q. 37** Explain the Relationship between materiality and audit risk.

(5 Marks, May, 2007) (4 Marks, November, 2014)

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### Relationship between Materiality and Audit Risk:

SA 320 on 'Materiality in Planning and Performing an Audit' requires that the auditor should consider materiality and its relationship with audit risk when conducting an audit.

In conducting an audit of financial statements, the overall objectives of the auditor are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and to report on the financial statements, and communicate as required by the SAs, in accordance with the auditor's findings.

The auditor obtains reasonable assurance by obtaining sufficient appropriate audit evidence to reduce audit risk to an acceptably low level.

Audit risk is the risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.

Materiality and audit risk are considered throughout the audit, in particular, when :

- a. Identifying and assessing the risks of material misstatement;
- b. Determining the nature, timing and extent of further audit procedures; and
- c. Evaluating the effect of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report.

### Author's Notes :

The auditor's preliminary assessment of materiality related to specific account balances and classes of transactions helps the auditor decide such questions as what items to examine and whether to use sampling and analytical procedures.

Materiality depends on the size and the nature of the items judged in the particular circumstances of its misstatement. The audit should be planned so that audit risk is kept at an acceptably low level. There is an inverse relationship between Materiality and the degree of audit risk. Higher the materiality level the lower the audit risk and vice-versa.

After the auditor has assessed the inherent and control risks, he should consider the level of detection risk that he is prepared to accept and, based upon his judgment, select appropriate substantive audit procedures. If the auditor does not perform any substantive procedures, detection risk, that is, the risk that the auditor will fail to detect a misstatement, will be high.

## Miscellaneous

**Q. 38 Write short notes on the following:**

**Matters that the auditor may consider when obtaining an understanding of the nature of the entity.**

(RTP IPCC Nov 15) (MTP Aug 2018, 4 Marks) (RTP IPCC Nov 15)

**Matters that the Auditor may consider when obtaining an understanding of the nature of the entity:** As per SA 315 "Identifying and Assessing the Risk of Material Misstatement through understanding the Entity and its Environment", following are some of the examples of matters that the auditor may consider when obtaining an understanding of the nature of the entity-

- i. **Business operations — such as:**
  - Nature of revenue sources, products or services, and markets, including involvement in electronic commerce such as internet sales and marketing activities.
  - Conduct of operations (for example, stages and methods of production, or activities exposed to environmental risks).
  - Alliances, joint ventures, and outsourcing activities.
  - Geographic dispersion and industry segmentation.
  - Location of production facilities, warehouses, and offices, and location and quantities of inventories.
  - Key customers and important suppliers of goods and services, employment arrangements.
  - Research and development activities and expenditures.
  - Transactions with related parties.

- ii. **Investments and investment activities — such as:**
  - Planned or recently executed acquisitions or divestitures.
  - Investments and dispositions of securities and loans.
  - Capital investment activities.
  - Investments in non-consolidated entities, including partnerships, joint ventures and special-purpose entities.
- iii. **Financing and financing activities — such as:**
  - Major subsidiaries and associated entities, including consolidated and non-consolidated structures.
  - Debt structure and related terms, including off-balance-sheet financing arrangements and leasing arrangements.
  - Beneficial owners (local, foreign, business reputation and experience) and related parties.
  - Use of derivative financial instruments.
- iv. **Financial reporting — such as:** Accounting principles and industry - specific practices, including industry - specific significant categories (for example, loans and investments for banks, or research and development for pharmaceuticals). Revenue recognition practices.
  - Accounting for fair values.
  - Foreign currency assets, liabilities and transactions.
  - Accounting for unusual or complex transactions including those in controversial or emerging areas (for example, accounting for stock-based compensation).

**Q. 39 List Various Documents to obtain Knowledge of Client's business.**

(RTP IPCC May 12)

**Knowledge of Client's Business:** As per SA 315, "Identifying and Assessing the Risk of Material Misstatement Through Understanding the Entity and its Environment" the auditor can obtain this information -

1. Clients annual report to shareholders;
2. Minutes of shareholders/board of directors;
3. Internal financial management reports of current & previous year;
4. Previous year audit working papers;
5. Discussion with client;
6. Clients policy and procedure manual;
7. Publications like trade journals, magazines, news papers; and
8. Visit to client's premises.

**Q. 40 Discuss the following**

**Despite of several disadvantages, audit programme is required to start an audit**

(5 Marks, November, 2013)

**OR**

**How does an audit programme help to plan and perform the audit?**

(5 Marks, May 2016) (RTP IPCC Nov 18, Nov 12)

**The Role of Audit Programme in Audit Plan and Performance /**

**Despite several disadvantages, Audit Programme is required to start an Audit:** Despite of several disadvantages, the audit programme is required to start an audit due to the following considerations-

1. The audit programme lists down areas of audit before commencement.
2. The audit timing is built therein; thereby it becomes a schedule of audit plan.
3. The staff who are entrusted with the audit assignment is also specified. It is a plan of resource allocation of the firm.
4. It specifies the procedures to be checked during the audit.
5. As the audit work is split into various elements of procedures to be performed, the audit programme acts as a guiding chart or check list during the performance of audit.
6. Since the staff in charge of each work is specified and they sign the programme, it extracts the responsibility from the audit assistants.





	<p>7. The working papers of the audit staff can be reviewed against the audit programme which helps a base of reference for evaluation of the performance before reporting on the financial statements.</p> <p>8. It also helps in preparing a diary of the performance and plan and also base for billing the clients for the time and manpower involved in the audit.</p>
<p><b>Q. 41</b></p>	<p><b>Describe a set of instructions, which an auditor has to give to his client before the start of actual audit.</b> (RTP IPCC Nov 14)</p> <p><b>Following instructions are given by the auditor to the client before the start of audit:</b></p> <ol style="list-style-type: none"> <li>1. The accounts should be total up and trial balance and final accounts to be kept ready.</li> <li>2. Vouchers should be serially arranged.</li> <li>3. Schedule of trade receivables and trade payables should be prepared.</li> <li>4. Schedule of outstanding expenses, prepaid expenses and accrued income to be kept ready.</li> <li>5. A list of bad and doubtful debts should be prepared.</li> <li>6. Schedule of investments should be prepared.</li> <li>7. Certified list of goods returned to be prepared.</li> <li>8. Statement of permanent capital expenditure to be prepared.</li> <li>9. Schedule of deferred revenue expenditures to be prepared.</li> <li>10. Names and addresses of managers and other officers should be kept ready.</li> </ol>
<p><b>Q. 42</b></p>	<p><b>State the factors which are to be considered in determining materiality.</b> (Nov, 15 -4 Marks)</p> <p><b>Factors to be considered for Determining Materiality:</b></p> <ol style="list-style-type: none"> <li>1. Item of materiality may be determined individually or in aggregate.</li> <li>2. The materiality depends on the regulatory or legal considerations.</li> <li>3. Materiality is not often reckoned with respect to quantitative details only. It has qualitative dimensions as well.</li> <li>4. Even insignificant items in terms of quality may be material in special circumstances.</li> <li>5. Sometimes the materiality of an item in terms of quantity is described in law itself. For example, Schedule III requires disclosure of items of expenditures which are in excess of one percent of the revenue from operations or ` 1,00,000, whichever is higher.</li> <li>6. An item whose impact is insignificant at present, but in future it may be significant, may be material item.</li> </ol> <p><b>Examiner Comment - Most of the examinees have no idea of the factors affecting materiality and gave mostly irrelevant points</b></p>
<p><b>Q. 43</b></p>	<p><b>Explain concept of materiality and factors which act as guiding factors to this concept.</b> (6 Marks, Nov. 2009) (RTP IPCC Nov 14)</p> <p style="text-align: center;"><b>OR</b></p> <p><b>“SA 320 “Materiality in Planning and Performing an Audit”, establishes standards on the concept of materiality and the relationship with audit risk while conducting an audit. Hence, the auditor requires more reliable evidence in support of material items”. Explain.</b> (RTP IPCC Nov 16)</p> <p><b>Concept of materiality: REFER Q31.</b></p> <p>A 320 on "Materiality in Planning and Performing an Audit" lays down the standard on the concept of materiality and its relationship with audit risk. As per SA 320 information is material if its mis-statement (i.e., omission or erroneous statement) could influence the economic decisions of users taken on the basis of the financial information.</p> <p>The concept of materiality recognises that some matters, either individually or in the aggregate, are relatively important for true and fair presentation of financial information in conformity with recognised accounting policies and practices.</p> <p>The auditor considers materiality at both the overall financial information level and in relation to individual account balances and classes of transactions. The concept of materiality recognizes that some matters, either individually or in the aggregate, are relatively important for true and fair presentation of financial information in conformity with recognised accounting policies and practices</p> <p><b>Factors to be considered for determining materiality: REFER Q42 .</b></p>



**Q. 44 State your views on the following requests made by the management of X Ltd.**

**“Auditor’s assessment of materiality may be different at the time of planning the engagement than at the time of evaluating the results of his audit procedures”. Discuss.**

(RTP IPCC Nov 12)

- **Auditor’s assessment of materiality:** SA 320 on “Materiality in Planning and Performing an Audit” recommends that 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.
- SA 450 “Evaluation of Misstatements Identified during the Audit”, 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.
- While formulating an overall audit plan, SA 300(Revised) on “Planning an Audit of Financial Statement” also requires the auditor to consider the setting of materiality levels for audit purpose right from the initial stages.
- Accordingly, the auditor has to assess the materiality aspect right from the initial stages. Accordingly, the auditor has to assess the materiality aspect right from the initial stages of audit planning and throughout the process of conducting the audit till the audit opinions is formulated.
- However, the auditor’s assessment of materiality may be different at the time of initially planning the engagement than at the time of evaluating the results of his audit procedures.
- Since audit materiality related to specific amount balances and classes of transactions, helps the auditor decide such questions as what items to examine and whether to use sampling and analytical procedures. This enables the auditor to select audit procedures that, in combination, can be expected to support the audit opinion at an acceptably low degree of audit risk. Such selection of audit procedures would undergo a change as audit work progress.
- The assessment of materiality and audit risk, the stage of evaluating the results of audit procedures would also change because of a change in circumstances or a change in the auditor’s knowledge as results of audit. For example, if the audit is planned prior to period end, the auditor will anticipate the results of operations and the financial position. If actual results of operations and financial position are substantially different, the assessment of materiality and audit risk may also change. Additionally, the auditor may, in planning the audit work, intentionally set the acceptable cut-off level for verifying individual transactions at a lower level than is intended to be used to evaluate the results of the audit. This may be done to cover a larger number of items and thereby reduce the likelihood of undiscovered misstatements and to provide the auditor with the measure of safety when evaluating the effect of misstatements discovered during the audit.

**Q. 45 An Auditor must take care to ensure that nothing is missed in the process which needs to be followed to achieve the audit objective. Explain the audit process with the help of a specimen.**

(RTP IPCC Nov 12)

**Audit process to ensure achievement of the Audit Objective**

The following audit process may be taken as a specimen to ensure that nothing is missed in the process which needs to be followed to achieve the audit objective:

- a. Formulating audit plan and laying down broad framework for conducting the work and method to ensure control over the quality of work.
- b. Examination and evaluation of the nature, extent and efficacy of the system of internal control. The nature, extent and timing of substantive procedures, would depend upon the extent of satisfaction an auditor obtains after evaluating the internal control system. The determination of extent of test checking would also depend upon the same.
- c. Ascertaining the arithmetical accuracy of the books of account by checking posting, casting, cross-casting, carry forwards, opening and closing balances, etc.
- d. Examining the documentary evidence (both internal and external) and the authority in support of the transaction, i.e. vouching.
- e. Checking the validity of transactions with reference to:
  - i. provisions affecting the accounts and audit in any Act or Rules;

- ii. rules and regulations governing the constitution and management of the organisation i.e., the memorandum and articles of association in the case of a company, partnership deed in the case of a firm, trust deed in the case of a trust and bye-laws in the case of a co-operative society;
- iii. minute book for appropriate sanction of the transactions by competent authority;
- iv. other legal documents such as the prospectus, returns submitted to legal authorities, contracts and agreements e.g., vendors' agreement, lease agreement, selling agency agreement, collaboration agreements, etc; and
- v. well recognised accounting principles and practices e.g., distinction between capital and revenue, accrual system of accounting, valuation principles, etc.,

Ensuring that there is adequate disclosure of information and, in particular, the annual accounts are prepared in such a manner as to convey the real picture about the assets and liabilities and of the operating result (profit or loss) of the organisation. For this purpose, the auditor must conform to the prescribed legal requirement, if any, as to the form of accounts and have due regard to the best current accounting practice. Reference to Revised Schedule VI in case of companies and compliance with accounting standards will have to be seen.

- a. Verification of existence, ownership, title and value of the assets and determination of the extent and nature of liabilities.
- b. Scrutiny of the accounts to establish reasonableness, consistency and compliance with the legal requirements
- c. Application of various overall checks in order to test the overall reliability of the accounting records and the statements and to see whether the results of overall checks corroborate the findings already made.
- d. Determination of the significant accounting ratios and subjecting the accounts to ratio analysis, to locate the areas, showing departure from the expected state of affairs.

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