

Chapter - 3 " Risk Assessment and Internal Control "

- Topics Covered:
- (1) Audit Risk (SA 315)
 - (2) Materiality in planning and performing an audit (SA 320)
 - (3) Identifying and Assessing ROMM (SA 315)
 - (4) Internal Control (SA 315)
 - (5) Risks that require special consideration
 - (6) Evaluation and Testing of Internal Control System
 - (7) Automated Environment
 - (8) Auditor's Responses to Assessed Risk (SA-330)

SA 200 - 299 - <u>General Principles</u>		⑥ SA 300 - 499 - Planning and Response ^{Risk}	
SA-200	SA-250 - X	SA-300 - <u>Planning</u>	450 - <u>Misstatements</u>
SA-210	SA-260 - <u>Truq</u>	✓ - 315 - <u>ROMM</u>	
SA-220	SA-265 - <u>Deficiency</u>	✓ - 320 - <u>Materiality</u>	
SA-230 - <u>" Audit Documentation "</u>	" in J.C.	✓ - 330 - <u>Responses to Assessed Risk</u>	
SA-240 - X	SA-299 - <u>Joint Audit</u>	- 402 - X	

(9) Misc. Topics:

- ✓(a) Manual and Automated Elements in J.C.
- ✓(b) Internal Financial Controls
- (c) Documenting the Risk
- (d) Assessing and Reporting of Audit findings

- From Book -

(a) Manual and Automated Controls:

- An Entity Internal Control System comprises of Manual and automated controls. Whether to use manual or automated controls, is a matter to be decided by the management, based on the Circumstances, level of automation etc.
- Manual controls include procedures like - Approval and Review of Transactions;
 - Reconciliations on periodic Basis;
 - Follow-up of Reconciling items; etc.
- Automated controls include General IT controls like controls over data centers and network operations, access security controls; and Application IT controls.
- Manual controls are considered more suitable where judgements are required, for example - (a) Unusual or non recurring transactions;
 - (b) Circumstances where error are difficult to predict or defined;
 - (c) Circumstances requiring response outside the scope of automated environment; And
 - (d) monitoring the effectiveness of automated Environment.
- Manual controls are considered less suitable in following cases:
 - (a) High Volume or recurring transactions;
 - (b) Situations where errors can be anticipated or predicted
 - (c) control activities where specific way to perform the control can be adequately designed and automated.

(b) Internal Financial Controls: Policies and procedures adopted by the company for ensuring :- Reliability of financial reporting;

- Efficiency and effectiveness of operations;
- Compliance with laws and regulations;
- Safeguarding of Assets; and

- Prevention and Detection of fraud and Error.

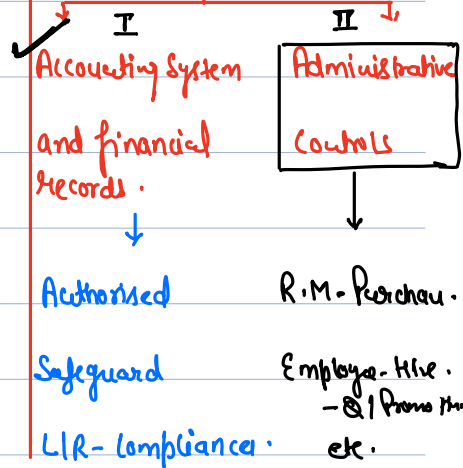
Statutory Requirements w.r.t. Internal financial Controls:

(A) Sec. 134(5): Listed Companies - Director's Responsibility statements.

Statement that the directors have laid down IFC to be followed by the company and such controls are adequate and operating effectively.

(Establish; Adequate; Effectively operate)

Internal control.



(B) Sec. 143(3)(i): Auditor is required to report whether company has adequate Internal controls w.r.t. financial statements in place and operating effectiveness of such controls.

(Existence and Adequacy; Effectively operate)

Exemption: Reporting not applicable in case of a private company which is

(a) OPC or Small Company; or

(b) having T/O < 50 Cr as per latest audited F.S. and aggregate borrowings from bank, F-I or Body Corporate at any point of time during the FY < 25 Cr.

* throughout the year

Puc ≤ 4 Cr + T/O ≤ 40 Cr

<u>Example</u>	<u>Company Type</u>	<u>Puc</u>	<u>Turnover</u>	<u>Max-ols Borrowing</u>	<u>Reporting</u>
A(P) Ltd.	OPC	Puc - 50 Lakh	Turnover - 51 Cr	B-Bank/FI/B.C-10 Cr	No
B(P) Ltd.	Other than OPC	Puc - 3 Cr	T/O - 35 Cr	Borrowing - 31 Cr	No (Small Co)
C(P) Ltd.	"	Puc - 5 Cr	T/O - 45 Cr	Borrowing - 26 Cr	YES
D(P) Ltd.	"	Puc - 3.99 Cr	T/O - 41 Cr	Borrowing - 24 Cr	No
E(P) Ltd.	"	Puc - 2 Cr	T/O - 49.8 Cr	Borrowing - 24.6 Cr	No
<u>FPO Ltd.</u>	"	Puc - 2.68 Cr	T/O - 35 Cr	Borrowing - 8 Cr	YES

(c) Sec. 177(4)(vii): Audit Committee: shall act in accordance with terms of reference as specified by Board, which shall include - Evaluation of IFC and Risk Mngt. System.

(d) Sec. 149(8): Company and Ind. directors shall abide by provisions specified in Schedule IV - [Code for Independent Directors]

↓
Role and Functions of Ind. directors.

↓
Ind. directors shall satisfy themselves - Integrity of financial information and that financial controls and risk mngt. system are robust and defensible.

(c) Documenting the Risk! (a) Discussion among ET and conclusions

(b) Key Elements of Understanding - Entity.

- Environment

- Components of I.C.

Source of info. from which understanding obtained;

RAP Performed.

(c) Identified and Assessed ROMM

(d) Identified Risk and related Controls

f.s. level

Assessment level.

(d) Assessing and Reporting - Audit findings: Learn Question from Q. Bank
(Noting - H.W.)