

# Chapter-3 "Audit Planning, Strategy and Execution"

Topics Covered: (1) Audit Process

(2) Using the work of Other Auditor (SA 600)

(3) " " " " Internal Auditor's (SA 610)

(4) " " " " Auditor's Expert (SA 620)

(5) Analytical Procedures (SA 520)

10 Sep →

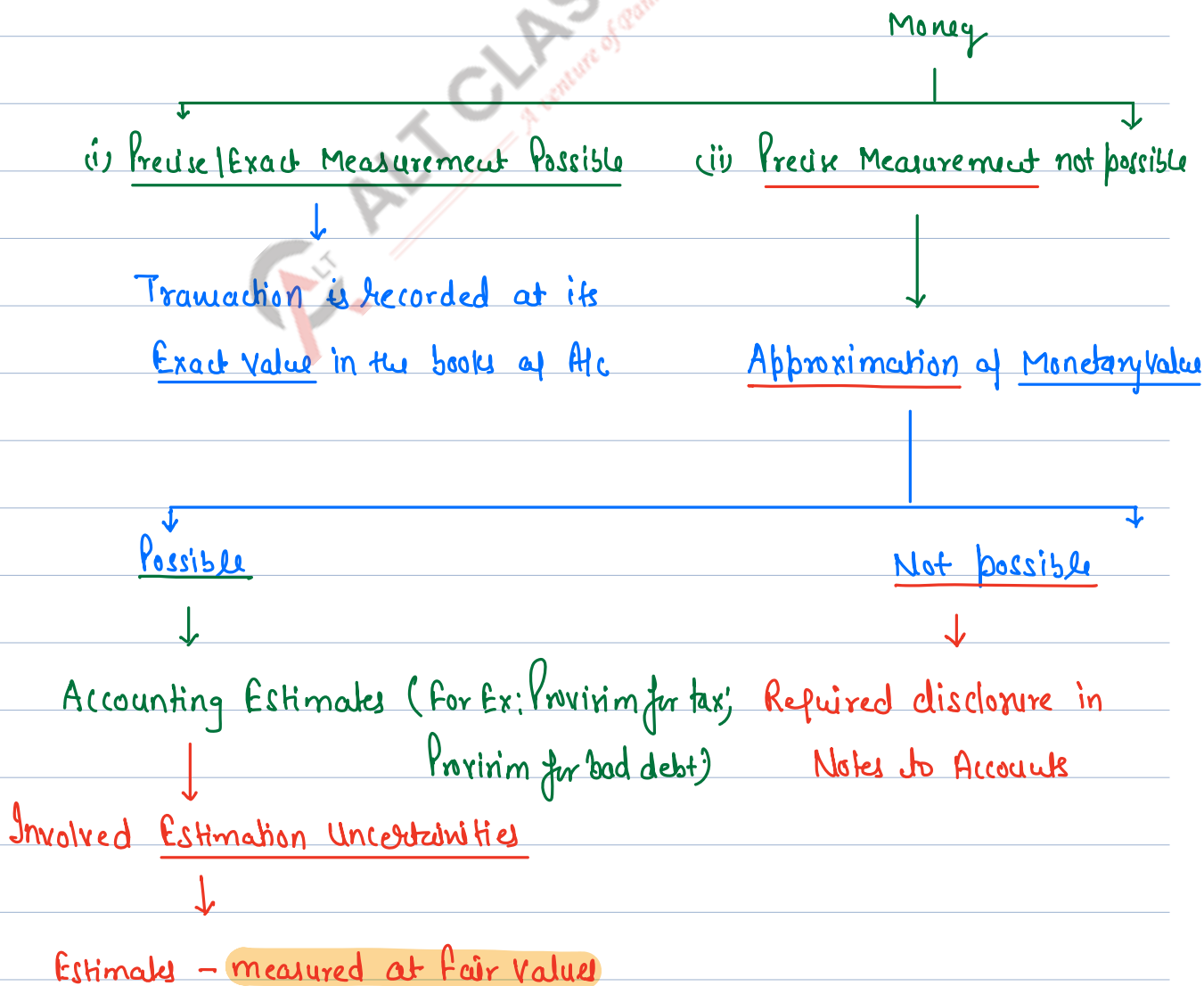
Monthly Test

Ch-1, 2, 3, 13, 19

50 Marks

(6) Auditing Accounting Estimates including fair value accounting estimates and related disclosures (SA 540):

Overview of Auditing Estimates: Events and transactions occurred → Measured in terms of



Meaning of Accounting Estimate: - Approximation of a monetary amount in the absence of precise means of measurement.  
 (As per SA-540)

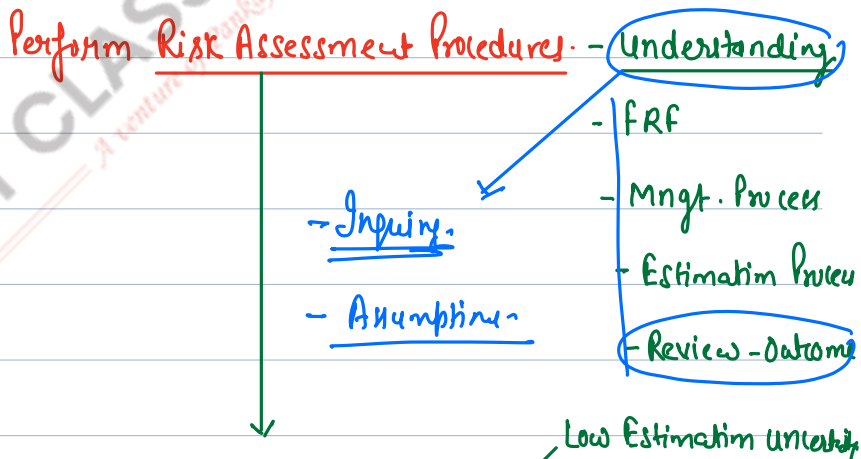
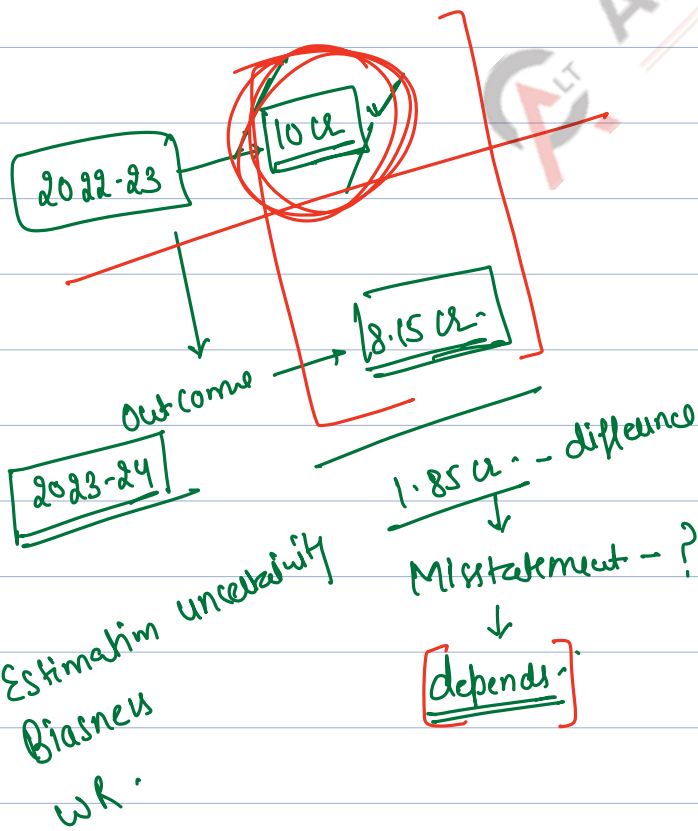
- This term is used for an amount measured at fair value where there is Estimation uncertainty. \*

\* Estimation Uncertainty: Susceptibility of an accounting estimate and related disclosures to an inherent risk of precision in the measurement.

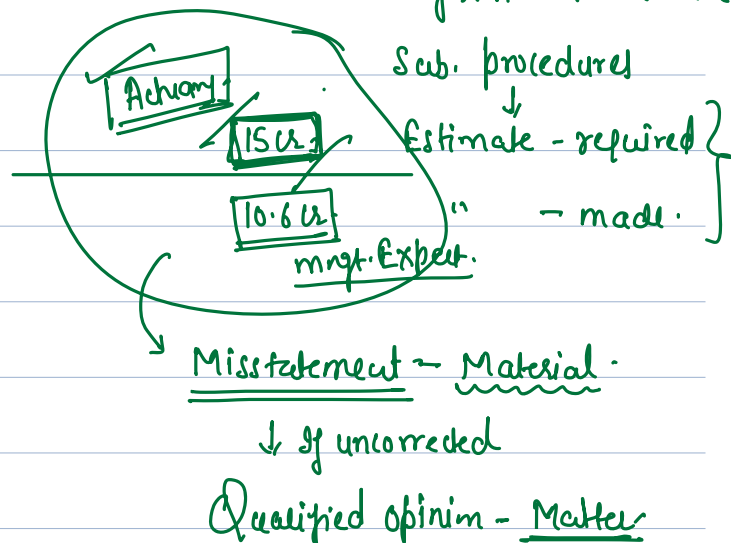
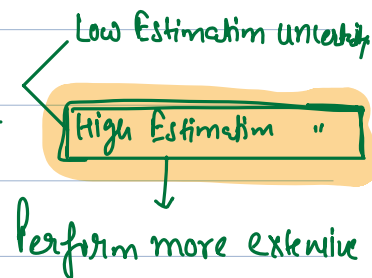
Examples of Accounting Estimates: - Reading from book -

Overview of Audit Procedures:

Perform Risk Assessment Procedures: - Understanding



Identify and Assess ROMM



## (A) Risk Assessment Procedure:

- Auditor should obtain an understanding of the following:

- (i) Requirements of applicable FRF;
- (ii) Mngt. process to Identify the transactions, events and conditions that may give rise to need for accounting estimates.
- (iii) Management Estimation making Process, including:
  - (a) Methods and Models Used;
  - (b) Use of Work of Management Expert;
  - (c) Relevant controls;
  - (d) Significant assumptions used;
  - (e) Changes in methods used from the prior period, along with reasons;
  - (f) How management assess the effect of Estimation Uncertainties.

✓ Auditor shall also review the outcome of accounting estimates of prior period.

Matters on which Inquiry is to made from management: LEARN + NOTING

- |                                |   |
|--------------------------------|---|
| (a) New Terms of transactions  | (a) changes in terms of transactions.             |
| (b) New Types of transactions. | (b) " " Accounting Policies due to changes in FRF |
| (c) New Conditions or Events   | (c) Changes in Regulatory Requirements.           |

Matters to be considered by auditor in obtaining understanding of assumptions

Used by Management: (a) Nature and Significance (e) Documentation

(Learning +  
Noting)

(b) Assessment of Relevancy and Completeness.

(c) Internally consistent

(d) Matter - within control of Mngt / outside the control.



## (B) Evaluation of degree of Estimation Uncertainty:

While identifying and assessing ROMM w.r.t. Accounting estimates, Auditor is required to evaluate degree of estimation uncertainty, associated with accounting estimates.

### Factors affecting degree of estimation uncertainty:

- (a) Extent to which estimates depends on judgement.
- (b) Sensitivity of accounting estimates to changes in assumptions.
- (c) Length of the forecast period.
- (d) Availability of reliable data from external sources.
- (e) Extent to which estimates are based on observable or unobservable inputs.
- (f) Existence of recognised measurement techniques that may mitigate the estimation uncertainty.

## (C) Responses to assessed risk:

Based on the understanding obtained and risks identified and assessed, Auditor shall determine:

- (i) whether management has applied the requirements of applicable FRF.
- (ii) whether management used the appropriate methods.
- (iii) " methods used are consistently applied.
- (iv) " changes, if any, in the accounting estimates or in the methods used for making them from prior period are appropriate.

For this purpose, Auditor shall perform Tests of Controls and Substantive procedures, as appropriate in the circumstances.

(D) Response to significant risk Estimation uncertainty: (e.g. Outcome of litigation)

For accounting estimates that give rise to significant risk, auditor shall evaluate the following:

- (i) How management has considered alternate assumptions available and why management rejected them.
- (ii) Whether the significant assumptions used are reasonable.
- (iii) Management intention to carry out specific course of action and their ability to do so

Ex: Provision towards Environmental liabilities and site clean-up cost:

Show - Cause Notice - Pollution Control Board

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[Non-compliance of Environmental laws and  
Imposing fine and penalties]

(E) Management Biasness: Lack of being neutral (by Mngt.) in preparing and presenting the financial and other information.

Auditor shall review the decisions and judgements taken by management in accounting estimates so as to identify possible management biasness.

Indicators of possible Management biasness: (Learning + Noting)

- (a) Change in Accounting Estimate / Method (b) Inconsistent assumptions (c) Assumptions - favorable for Mngt. objectives (d) Point Estimate - Optimism / pessimism.

(F) Written Representations: (Learning + Noting) - (Self study H.W.)