

10. ANALYTICAL PROCEDURES**QUESTION - WISE ANALYSIS OF PREVIOUS EXAMINATIONS**

No.	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
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Q.No.1. What are Analytical Procedures as per SA 520. Explain with examples? (C) (NEW SM)

MEANING:

As per the SA-520:

- a) "Analytical Procedures", means evaluations of financial information through analysis of plausible (acceptable) relationships among both financial and non-financial data.
- b) Analytical procedures include
 - i) Investigating fluctuations or
 - ii) Relationships that are inconsistent with other information (or) which differ from expected values by a significant amount.
 - iii) It also includes comparison of financial statements with consideration of relationships.

EXAMPLES:

1. Comparison of entity's Financial information -
 - a) Comparable information for prior periods
 - b) Anticipated results of the entity, such as budgets or forecasts.
 - c) Similar Industry information concerning the entity such as industry average.
2. Consideration of relationships -
 - a) Among elements of financial information that would be expected to conform to a predictable pattern based on the entity's experience, such as gross margin percentages.
E.g. An increase in sales must lead to increase in profit of the entity. (Margin of safety)
 - b) Between financial information and relevant non-financial information, such as payroll costs to number of employees.
E.g. An increase in number of employees may lead to increase in earnings.
3. Thus analytical procedure broadly cover these types of comparison -
 - a) Comparison of Client and Industry data.
 - b) Comparison with prior period data.
 - c) Comparison with expected results.
 - d) Comparison with auditors expected results.
 - e) Comparison of Financial and Non-Financial data.

SIMILAR QUESTION:

1. Define Analytical Procedures A. Refer meaning	NEW SM - TYK
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Q.No.2. What is the purpose of analytical procedures? (B)

(NEW SM)

Analytical procedures use comparisons and relationships to determine whether account balances or other data appear to be reasonable.

ANALYTICAL PROCEDURES ARE USED FOR THE FOLLOWING PURPOSES:

- i) To obtain relevant and reliable audit evidence when using substantive analytical procedures; and
- ii) To design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are in consistent with auditor's understanding about the entity.

E.g. In XYZ Ltd., after applying analytical procedures as comparison of the gross profit ratio with that of the previous year, it is discovered that there has been fall in the ratio. Therefore, it became necessary for the auditor to make further enquiries as it may be due to pilferage of inventories/ misappropriation of a part of the sale proceeds/ a change in the cost of sales without a corresponding increase in the sales price.

CONCLUSION: Thus, it is important to note that Analytical procedures may help identify the existence of unusual transactions or events, and amounts, ratios, and trends that might indicate matters that have audit implications.

SIMILAR QUESTIONS:

1. Analytical procedures use comparisons and relationships to assess whether account balances or other data appear to be reasonable. Explain stating the purpose of analytical procedures with examples.	RTP M18(N)
A. Refer above answer	

Q.No.3. Write about Timing of Analytical procedures? (A)

(NEW SM)

Analytical Procedures are used in three stages.

1. Planning Phase
2. Testing Phase
3. Completion Phase

DURING PLANNING PHASE:

1. In the planning stage, analytical procedures help the auditor in understanding the client's business and in identifying areas of potential risk by indicating aspects of and developments in the entity's business of which he is previously unaware.
2. This information will assist the auditor in determining the nature, timing and extent of his other audit procedures.
3. Analytical procedures in planning the audit use both financial data and non-financial information.

SIMILAR QUESTIONS:

1. Analytical Procedures are used in various phases of an audit, especially at planning stage. Explain?	
A. Refer above answer	

Q.No.4. Write a short note on substantive analytical procedures? (B)

(NEW SM)

1. Substantive procedure includes Test of Details and Analytical Procedures. Therefore analytical procedures are one of the substantive audit procedures.
2. When to use substantive analytical procedures: It is based on the auditor's judgment so as to reduce audit risk to an acceptably low level.

3. The auditor may inquire of management as to the availability and reliability of information needed to apply substantive analytical procedures, and also inquire the results of any such analytical procedures performed by the entity.
4. While carrying out the analytical procedures the auditor can use the analytical data prepared by management provided he verified its authenticity.

SIMILAR QUESTIONS:

1. Nature and extent of carrying substantive procedures is a matter of professional judgment of auditor? Explain. Also explain meaning of Substantive analytical procedures? A. Write Meaning Given in Q No 1 and then above answer.	
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Q.No.5. Explain the Techniques Available as Substantive Analytical Procedures? (A) (NEW SM)**A. TREND ANALYSIS:**

1. A commonly used technique is the comparison of current data with the prior period balance or with a trend in two or more prior period balances.
2. We evaluate whether the current balance of an account moves in line with the trend established with previous balances for that account

B. RATIO ANALYSIS:

1. Ratio analysis is useful for analysing asset and liability accounts as well as revenue and expense accounts.
2. An individual balance sheet account is difficult to predict on its own, but its relationship to another account is often more predictable
3. Financial ratios may include:
 - a) Trade receivables or inventory turnover
 - b) Freight expense as a percentage of sales revenue

C. REASONABLENESS TESTS:

These Procedures does not rely on events of prior periods, but upon non-financial data for the audit period under consideration. These tests are generally more applicable to income statement accounts while determining revenue and expenses.

D. STRUCTURAL MODELLING:

A modelling tool constructs a statistical model from financial and/or non-financial data of prior accounting periods to predict current account balances. (E.g., It is a combination of various statistical tools such as regression, path analysis etc. It is most unused tool due to its complex process and involvement of statistical technological tools).

SIMILAR QUESTIONS:

1. "The design of a substantive analytical procedure is limited only by the availability of reliable data and the experience and creativity of the audit team. Substantive analytical procedures generally take certain forms" Explain the various forms. A. Write above answer.	MTP N18(N)
2. Explain the Techniques Available as Substantive Analytical Procedures? A. Write above answer.	RTP M19(N)
3. Ratio analysis is useful for analysing asset and liability accounts as well as revenue and expense accounts. An individual balance sheet account is difficult to predict on its own, but its relationship to another account is often more predictable (e.g., the trade receivables balance related to sales). Explain stating the techniques available as substantive analytical procedures. A. Write above answer.	RTP M18(N)
4. Discuss the techniques available as Substantive Analytical Procedures A. Write above answer.	M18(N) - 5M

**Q.No.6. Write about suitability of particular analytical procedures for given assertions? (A)
(NEW SM)**

1. Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time.
2. However, the suitability of a particular analytical procedure will depend upon the auditor's assessment of how effective it will be in detecting a misstatement that may cause the financial statements to be materially misstated.
3. In some cases, even an unsophisticated predictive model may be effective as an analytical procedure.
4. Further different analytical procedures provide different levels of assurance.
5. Example - If an entity has a known number of employees at fixed rates of pay throughout the period, it may be possible for the auditor to use this data to estimate the total payroll costs for the period with a high degree of accuracy, thereby providing audit evidence for a significant item in the financial statements and reducing the need to perform tests of details on the payroll.

SIMILAR QUESTIONS:

1. Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. Explain. A. Refer above answer	MTP M19 (N), RTP N18 (N)
2. While carrying out the statutory audit of a large entity, what are the substantive procedures to be performed to assess the risk of material misstatement? A. Refer above answer	NEW SM

**Q.No.7. Extent of reliance on analytical procedures is influenced by its nature and source. Explain? (B)
(NEW SM)**

The reliability of data is influenced by its source and nature. Accordingly, the following are relevant when determining whether data is reliable for purposes of designing substantive analytical procedures:

A. SOURCE:

Information may be more reliable when it is obtained from independent sources outside the entity;

B. COMPARABILITY:

Broad industry data may need to be supplemented to be comparable to that of an entity that produces and sells specialised products

C. NATURE AND RELEVANCE:

Whether budgets have been established as results to be expected rather than as goals to be achieved

D. CONTROLS OVER THE PREPARATION OF THE INFORMATION:

The auditor considers testing the operating effectiveness of controls over the entity's preparation of information used by the auditor in performing substantive analytical procedures in response to assessed risks.

When such controls are effective, the auditor generally has greater confidence in the reliability of the information and in the results of analytical procedures.

SIMILAR QUESTIONS:

1. The reliability of data is influenced by its source and nature and is dependent on the circumstances under which it is obtained. Accordingly, explain the factors are relevant when determining whether data is reliable for purposes of designing substantive analytical procedures. A. Refer above answer	MTP1 N18(N), MTP1 M18 (N)
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2. What are the factors that determine the extent of reliance that the auditor places on results of analytical procedures? Explain with reference to SA-520 on "Analytical procedures". A. Refer above answer	NEW SM - TYK
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Q.No.8. Write a short note on matters relevant to the auditor's evaluation risk of material misstatements? (B) (NEW SM)

- The accuracy with which the expected results of substantive analytical procedures can be predicted.
Example: The auditor may expect greater consistency in comparing gross profit margins from one period to another than in comparing discretionary expenses, such as research or advertising.
- The degree to which information can be disaggregated.
Example: Substantive analytical procedures may be more effective when applied to financial information on individual sections of an operation or to financial statements of components of a diversified entity, than when applied to the financial statements of the entity as a whole.
- The availability of the information, both financial and non-financial.
Example: The auditor may consider whether financial information, such as budgets or forecasts, and non-financial information, such as the number of units produced or sold, is available to design substantive analytical procedures. If the information is available, the auditor may also consider the reliability of the information.

SIMILAR QUESTION:

1. "Matters relevant to the auditor's evaluation of whether the expectation can be developed sufficiently precisely to identify a misstatement that, when aggregated with other misstatements, may cause the financial statements to be materially misstated" Explain with examples. A. Refer above answer	
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Q.No.9. How to deal with investigating results of analytical procedures? (B) (NEW SM)

A. INQUIRING OF MANAGEMENT:

Audit evidence relevant to management's responses may be obtained by evaluating those responses taking into account the auditor's understanding of the entity and its environment, and with other audit evidence obtained during the course of the audit.

B. PERFORMING OTHER AUDIT PROCEDURES:

The need to perform other audit procedures may arise when, for example, management is unable to provide an explanation, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate.

SIMILAR QUESTIONS:

1. "If analytical procedures performed in accordance with SA 520 identify fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount, the auditor shall investigate such differences" Explain. A. Refer above answer	RTP M19(N)
2. While performing analytical procedures on financials of ABC limited, the auditor identifies fluctuations or relationships that are inconsistent with other relevant information and also that differs from expected values by a significant amount. The auditor seeks your advice as to how should he proceed. A. Refer above answer	MTP M18(N)

QUESTIONS FOR ACADEMIC INTEREST - FOR STUDENT'S SELF STUDY

Q.No.10. What are the considerations specific to public sector entities with respect to analytical procedures? (C) (NEW SM)

The relationships between individual financial statements items traditionally considered in the audit of business entities may not always be relevant in the audit of governments or other non-business public sector entities;

For example, in many public sector entities there may be little direct relationship between revenue and expenditure. In addition, because expenditure on the acquisition of assets may not be capitalized, there may be no relationship between expenditures on, for example, inventories and fixed assets and the amount of those assets reported in the financial statements.

Also, industry data or statistics for comparative purposes may not be available in the public sector. However, other relationships may be relevant, for example, variations in the cost per kilo meter of road construction or the number of vehicles acquired compared with vehicles retired.

SIMILAR QUESTION:

<p>1. The relationships between individual financial statements items traditionally considered in the audit of business entities may not always be relevant in the audit of governments or other non-business public sector entities. Analyse and Explain.</p> <p>A. Refer above answer</p>	<p>RTP N18(N)</p>
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Q.No.11. While carrying out the statutory audit of a large entity, what are the substantive procedures to be performed to assess the risk of material misstatement? (C) (NEW SM - TYK)

Substantive Procedures to be performed to assess the risk of material misstatement:

As per SA 330, "The Auditor's Response to Assessed Risk", substantive procedure is an audit procedure designed to detect material misstatements at the assertion level.

It consist tests of details and substantive analytical procedures.

- a) Test of Details:** The nature of the risk and assertion is relevant to the design of tests of details.
Example:
- i) Tests of details related to the existence or occurrence assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence.
 - ii) Tests of details related to the completeness assertion may involve selecting from items that are expected to be included in the relevant financial statement amount and investigating whether they are included.
 - iii) In designing tests of details, the extent of testing is ordinarily thought of in terms of the sample size.
- b) Substantive Analytical Procedures:**
- i) Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time.
 - ii) The application of planned analytical procedures is based on the expectation that relationships among data exist and continue in the absence of known conditions to the contrary.
 - iii) However, the suitability of a particular analytical procedure will depend upon the auditor's assessment of how effective it will be in detecting a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated.
 - iv) In some cases, even an unsophisticated predictive model may be effective as an analytical procedure.
 - v) The use of widely recognised trade ratios can often be used effectively in substantive analytical procedures to provide evidence to support the reasonableness of recorded amount.

Q.No.12. What are the Factors to be considered for Substantive Audit Procedures? (C) (NEW SM)

The auditor should consider the following factors for Substantive Audit Procedures:

- a) **Availability of Data:** The availability of reliable and relevant data will facilitate effective procedures.
- b) **Disaggregation:** The degree of disaggregation in available data can directly affect the degree of its usefulness in detecting misstatements
- c) **Account Type:** Substantive analytical procedures are more useful for certain types of accounts than for others.
 - i) Income statement accounts tend to be more predictable because they reflect accumulated transactions over a period.
 - ii) Balance sheet accounts represent the net effect of transactions at a point in time or are subject to greater management judgment.
 - iii) We can analyse data to understand the relationship to another account and through this, disaggregate the transactions flowing to and from the balance sheet account (e.g., sales and cash receipts flowing through trade receivables), or to compare ratios over time as this enhances our ability to obtain audit evidence for balance sheet accounts.
- d) **Source:** Some classes of transactions tend to be more predictable because they consist of numerous, similar transactions, (e.g., through routine processes). Whereas the transactions recorded by non-routine are more difficult to predict.
- e) **Predictability:** Substantive analytical procedures are more appropriate when an account balance or relationships between items of data are predictable. A predictable relationship is one that may reasonably be expected to exist and continue over time.
- f) **Nature of Assertion:** Substantive analytical procedures may be more effective in providing evidence for some assertions (e.g., completeness or valuation) than for others (e.g., rights and obligations). Predictive analytical procedures using data analytics can be used to address completeness, valuation/measurement and occurrence.
- g) **What Can Go Wrong (WCGW):** When we are designing audit procedures to address an inherent risk or “what can go wrong”, we consider the nature of the risk of material misstatement in order to determine if a substantive analytical procedure can be used to obtain audit evidence. When inherent risk is higher, we may design tests of details to address the higher inherent risk. When significant risks have been identified, audit evidence obtained solely from substantive analytical procedures is unlikely to be sufficient.

SIMILAR QUESTION:

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| <p>1. “The auditor’s substantive procedures at the assertion level may be tests of details, substantive analytical procedures, or a combination of both. The decision about which audit procedures to perform, including whether to use substantive analytical procedures is based on the auditor’s judgment about the expected effectiveness and efficiency of the available audit procedures to reduce audit risk at the assertion level to an acceptably low level” Explain the factors that are to be considered while performing such tests.</p> <p>A. Refer above answer</p> | |
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Q.No.13. Write about suitability of Analytical Procedures used as Substantive Tests? (C) (NEW SM)

1. Determine the suitability of particular substantive analytical procedures for given assertions, taking account of the assessed risks of material misstatement and tests of details
2. Evaluate the reliability of data from which the auditor’s expectation of recorded amounts or ratios is developed, taking account of source, comparability, and nature and relevance of information available, and controls over preparation.

3. Develop an expectation of recorded amounts or ratios and evaluate whether the expectation is sufficiently precise to identify a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated; and
4. Determine the amount of any difference of recorded amounts from expected values that is acceptable without further investigation.

SIMILAR QUESTIONS:

1. "When designing and performing substantive analytical procedures, either alone or in combination with tests of details, as substantive procedures in accordance with SA 330, the auditor shall follow various audit procedures" Explain such procedures. A. Refer above answer	
2. How to use analytical procedures as substantive tests? A. Refer above answer.	

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