/01/24

CH-3

Risk Assessment & Internal Control

Digital Audit

↓

Automated Environment

↓

It Related RIsks

↓

Controls & Types of IT Controls

↓

Impact on Controls

↓

Internal financial Decision Contro

↓

Data Analytics

↓

Testing Methods

↓

SA 315, SA 320 & SA 330

↓

1. Audit Risk

Audit risk means risk that auditor gives an inappropriate audit opinion when the Financial Statements are materially misstated.

It means that an auditor expresses an unmodified opinion when Financial Statements are materially misstated.

SA-200 states that auditor shall obtain Sufficient appropriate audit evidence to reduce audit risk to an acceptably low level and therby enable auditor to draw reasonable's conclusions on wh to base auditor's opinion

Risks of Material misstatement

SA-200 states that risk of material statement is the risk that financial Statements are materially misstated prio to audit. It simpey means that there is a probability of frauds or errors in financial Statements befor Audit

1) financial statement level

2) Assertion level

Components of RMM

1) Inherent Risk

It is a risk that Class of transaction, account balance could be materialy misstated either individually or aggregated with other misstatement before consideration related control.

Inherent risk may be higher for some assertion as compare to others. Inherent risk factors are considered while TOC (Test of Controls) and substantive procedures external circumstances which may also effect inherent risk

2) Control Risk

Control risk is the risk that misstatement that could in assertion about a class of transaction, account balance or disclosure that could be material either individually or when aggregated with other misstatments,

will not be prevented, detected and corrected on a timely basis by the entity's control.

Inverse relation exist between Control risk and efficiency of Control risk.

Note → when efficiency of Internal Control of an entity is high ↑
Control risk is low ↓

When efficiency of Internal Control of an entity is ~~high~~ ↑ Low ↓
Control risk is high ↑

1.3 Detection Risk

It is a risk that Procedure perf by auditor to reduce risk to an acceptly low level will not detect mistatment that exists that could be, either individually or when aggregated with other misstatements.

Types

1) Sampling Risk - Risk that Auditor conclusion based on Sample may different from Conclusion entire po if they were Suject Same Audi procedures. It means Sample was representative of Population from it was chosen.

AI QUAD CAMERA
Shot on realme 5i
2024/10/11 20:35

2) NON Sampling risk--It means auditor reaches an erroneous Conclusion for any reason not related to Sampling risk. However risk that auditor is due to Application to some inappropriate audit procedure.

△ Auditor Can Only Influence detection risk

△ IR & CR belong to entity Can be influenced by Entity.

△ Auditor Must Reduce detection risk in order to keep audit Risk at low level.

△ Detection risk may be reduced by
e Increasing area of Checking, testing ledger including Competent and experiencing engagement team

△ What is not included in Audit Risk

- Audit risk does not refer to Business risk.

o Such as laws of litigation, Adverse Publicity etc

- It also do not include Auditor might express opinion that f.S materialy misstate when Infact their not.

1.5 Assessment of Risks – A matter of professional Judgement.

1. Audit risk is the function of risk of material misstatement and detection risk.

2. Assesment of risk is based on Audit procedures which are applied to obtain Audit evidence so that important information can be used

3. It is expected that professional Judgement exercise by auditor whose traing, knowledge, experience have assisted in developing necessary competencies to achieve reasonable Judgements

Combined assesment of risk mistatement

SA do not refer IR and CR Seprately but rather combined Rmm refered However Auditor may make seprate & combined assesment prefered audit techni methodlogies, practical considerations

2. Assessment of Rmm can be in quantitative & qualitative terms

3. AR = IR × CR × DR

1.6 Identifying and assessing Rmm

1. SA 315 Identifying & assessing Rmm through understanding the entity and its environment including control

2. Objective is to as Identifying assess Rmm at FS and Assertion level

3. It will help in Providing basis for deciding designing and Implementing responses to assessed risk of rmm.

4. It will help to reduce risk acceptable low level.

Objective as per SA 315

1. Auditor shall Identify Rmm FS level & Assertion level

2. To provide basis for designing & performing further audit procedures

For purpose of Identifying and assess Rmm auditor shall -

1) Identify risks by understanding entity and its environment Including IT at FS and assertion level

2) Identified risks and evaluate whether they effect more pervasively to F.S or affect many assertions

3) Identify what can go wrong at assertion level.

4) Consider likehood of statement Including multiple misstatement whether potential statement magnitude that could result in MM.

[SA 320 materiality in planning and performing an Audit.]

Observation & Inspection - It supports Inquiries of management and others which provide Information about entity and its environment

Information obtained by RAP

1. It can be used as Audit evidence audit may obtain various assertions and operating effectiveness of controls even if through procedures or ToC

Materiality

SA 320 Materiality in planning & performing an audit

Risk assesment Procedures

The audit procedure Performed to obtain an understanding of entity and its environment Including IC to Identify & assess Rmm, whether due to fraud or error at FS level and assertion level.

What is Included in RAP

a. Inquiries of management and others within entity.

b) auditor can obtain Information management & others and those who are responsible for Prepration of Financial Reporting. However Auditor may also

Inquires from other employees within entity.

AI QUAD CAMERA
Shot on realme 5i
2024/10/11 20:36

IX Analytical Procedure

It helps in Identfying aspects of the entity of which auditor was unaware may assist in assesing RMM in order to provide designing & Implementation responses to assessed risks.

It may include both Financial & non financial data.

It may help Identify unusual transactions or events, ratios and trends that might indicate matters that have audit Implicatio

2. MATERIALITY

1. It states that misstatement including omissions are considered to be material if they Individually or aggregate could reasonably be expected to Influence the economic decisions of users of F.S.

2. The objective of auditor RA-FS-FF-M whether due to fraud or error whi enables auditor to express opinion on that they are prepared all materia expects as applicable FRF.

3. Materiality is not always matter of relative size.

IV Materiality in planning & performing an audit Auditor's Responsibility -

Concept of Materiality is applied by auditor in both performing & planning & in evaluating effect of Identified misstatements on Audit and uncorrected misstatements on FS and on Audit report.

2. Often FRF preparing affect

3. Revision in materiality level as the Audit progresses

As Circumstances change during the Audit Auditor May its change materiality level if there is significant difference Actual F. Results substantially different from anticipated period revise Materiality

Documenting the materiality

1) materiality as a whole
2) materiality class of transactions, account balances disclosure
3) Performance Materiality
4) Any changes

AI QUAD CAMERA
Shot on realme 5i
2024/10/11 20:36

They are considered in particular when Identifying RMM

Determining the NTE further Audit procedures

Evaluating effect of uncorrected misstatements on financial statements

3. Understanding the Entity & its Environment

a) Relevant Industry, Regulatory and other External factors including applicable FRF

Industry factors as Technological developments and Customer Relationship.

b) Regulatory factors such as FRF legal & ~~political~~ environment

Nature of entity

i) its Operations

ii) ~~Operations~~ ownership & governance Structures

iii) The types of Investments entity making and plans to make

iv) How entity Structured & finance whether entity is a complex ... Can be identified by understanding Na...

c) The entity's selection and application of Accounting policies including changes

The auditor shall evaluate whether entity's accounting policies are appropria for its business and consistent with applicable FRF

d) Entity's objectives, strategies those business risk that may result in RMM

Management defines objectives which overall plan for the entity.

c) Business risk is broder than RMM and includes latter.

Those Business risk which have financial are relevent auditor determing RMM

e) The measurement & review of the entity's financial perfomance

Perfomance measures whether Internal or external create pressure on entity

management takes Action to improve perfomance considering whether pressu to achieve target may result in management actions.