

# 2

## CHAPTER

# Audit Strategy, Audit Planning and Audit Programme

### ■ AUDITOR'S RESPONSIBILITY TO PLAN AN AUDIT OF FINANCIAL STATEMENTS

SA 300 "Planning an Audit of FS"

Objective of the Auditor to plan an Audit



So that it can be performed Effectively



Timely Manner

SA 300 Planning an audit of financial statements deals with the auditor's responsibility to plan an audit of financial statements. It states that objective of the auditor is to plan the audit so that it will be performed in an effective manner.

### QUESTIONS

#### Multiple Choice Questions (MCQ)

1. Which of the following is not considered in planning an audit generally?
  - (a) Understanding of legal and regulatory framework of an entity
  - (b) Need to consider determination of materiality
  - (c) Evaluating audit evidence
  - (d) Need to consider involvement of expert

**Ans.** (c) Evaluating audit evidence

#### Notes to Add

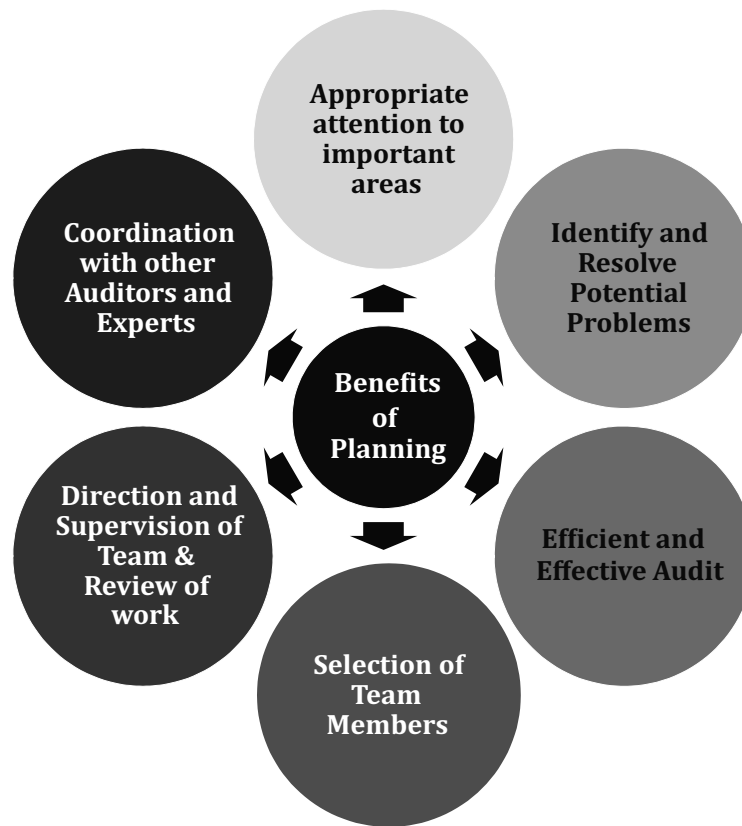
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**QUESTIONS**

**Correct/Incorrect**

**State with reasons (in short) whether the following statements are correct or incorrect:**

1. Once the audit plan has been drafted and communicated, it is obligatory on the auditor to follow the same.

**Ans. Incorrect:** 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.

**Notes to Add**

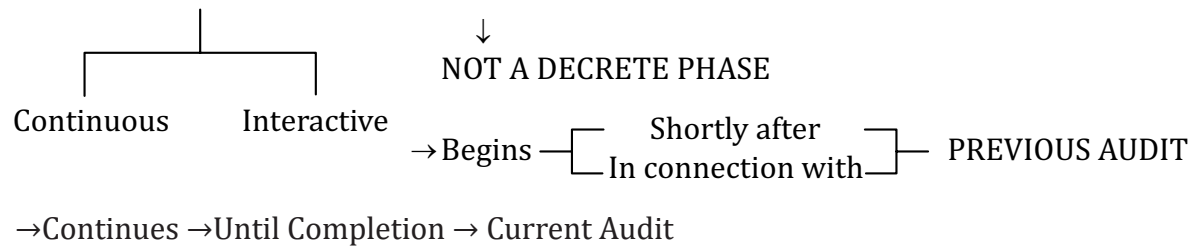
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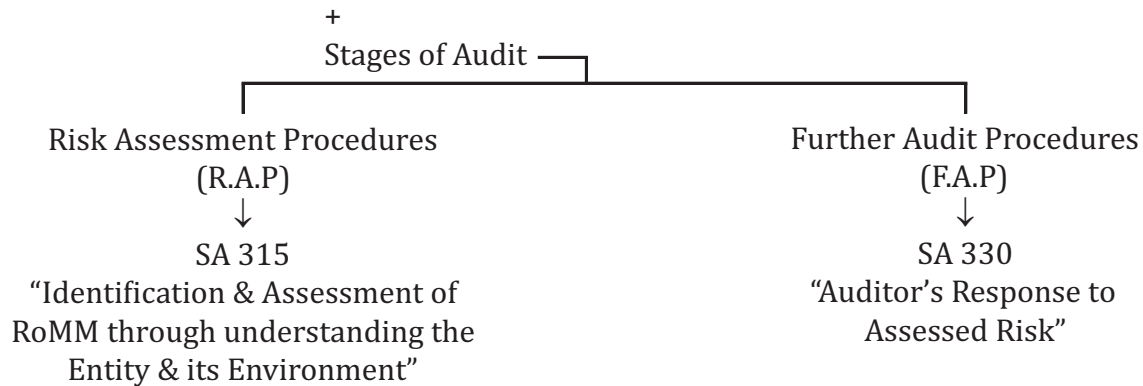
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## ■ NATURE OF AUDIT PLANNING



→EXTRA GYAAN →Audit Procedures



└ Things to be done before R.A.P. → Consider

- (1) Analytical Procedures → to be applied as → RAP
- (2) General Understanding Entity Complying } LEGAL + REGULATORY Framework
- (3) Determination of Materiality
- (4) Involvement of Experts → Taking A/c. of Complexity of Business
- (5) Performance of other RAP

Planning Involves — Engagement Partner — Experience  
 — Other key Members — Insight  
 • Enhance Eff. & EFF.

DISCUSSION OF ELEMENTS OF PLANNING → with Mgt.

↓  
Auditor May Discuss → To — Facilitate — of Audit Engagement  
 ↓ Conduct

NOT TO COMPROMISE THE EFFECTIVENESS OF AUDIT

### Notes to Add

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## ■ NATURE OF AUDIT PLANNING-A CONTINUOUS AND ITERATIVE 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.

Risk assessment procedures are audit procedures performed to obtain an understanding of the entity and its environment, including the entity's internal control, to identify and assess the risks of material misstatement, whether due to fraud or error at the financial statement and assertion levels.

Therefore, planning includes consideration of matters such as obtaining knowledge about legal framework in which entity is operating. Consider for example- Telecom companies and Banks. Such entities operate in different legal and regulatory frameworks. TRAI (Telecom Regulatory Authority of India) and RBI (Reserve Bank of India) are regulators for telecom and banking industry respectively.

Planning also includes need to consider determination of material or significant matters. It also involves considering whether experts need to be involved taking into account complexity of business. Further, it also involves considering need to perform risk assessment procedures for identifying and assessing risks of material misstatement.

Planning is not a separate or distinct phase of an audit. It is to be viewed as a continual and repetitive process. It is a continuous process that begins with completion of previous audit and continues till the completion of current audit engagement.

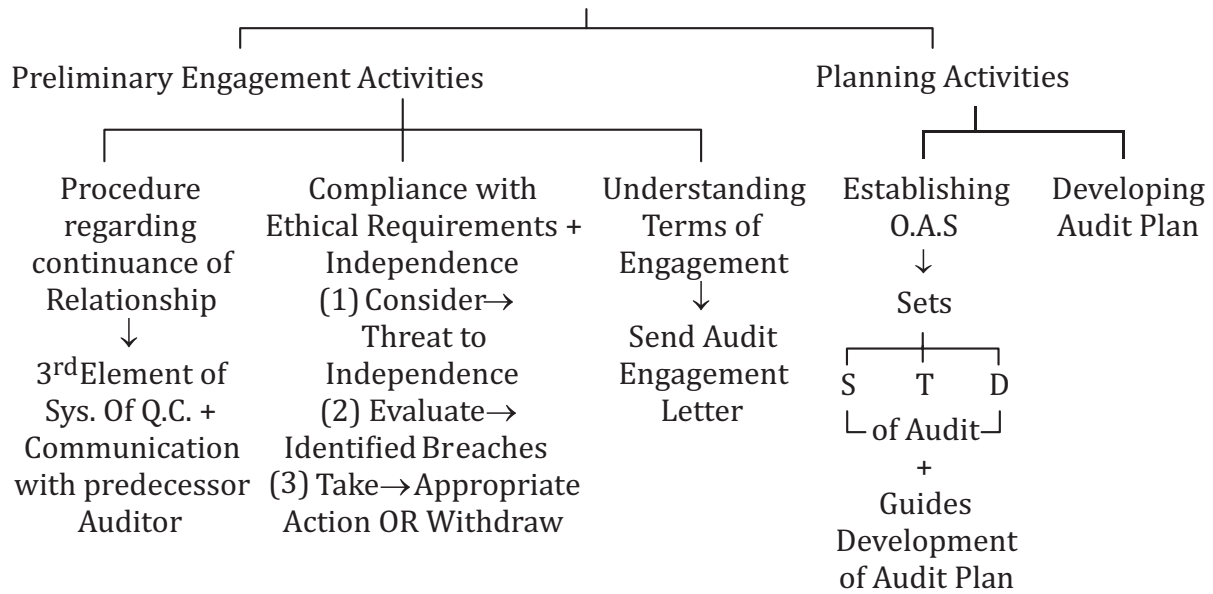
## ■ INVOLVEMENT OF KEY ENGAGEMENT TEAM MEMBERS IN PLANNING AUDIT

The engagement partner and other key members of the engagement team shall be involved in planning the audit including planning and participating in the discussion among engagement team members. The involvement of the engagement partner and other key members of the engagement team in planning the audit draws on their experience and insight, thereby enhancing the effectiveness and efficiency of the planning process.

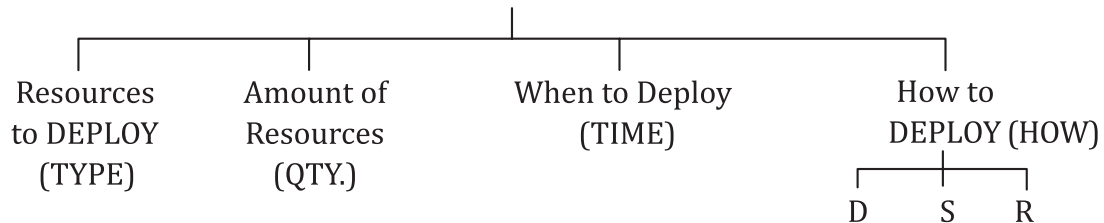
## ■ DISCUSSION OF ELEMENTS OF PLANNING WITH ENTITY'S MANAGEMENT

The auditor may decide to discuss elements of planning with the entity's management to facilitate the conduct and management of the audit engagement. When discussing matters included in the overall audit strategy or audit plan, care is required in order not to compromise the effectiveness of the audit.

## ■ PLANNING PROCESS ELEMENTS OF PLANNING

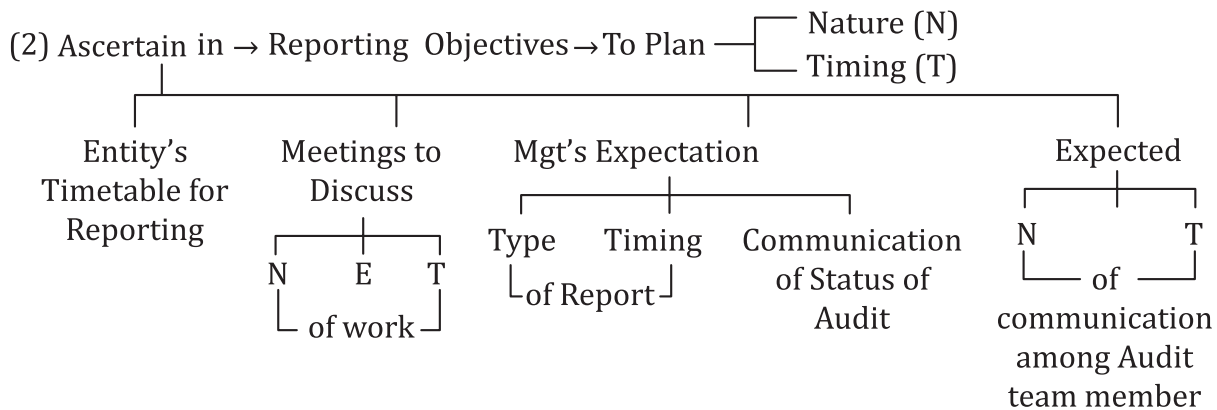
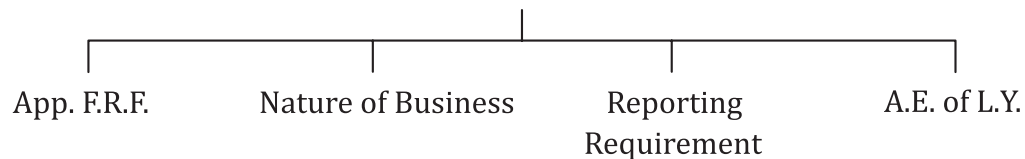


OAS → Assist Auditor → To Determine → AFTER R.A.P

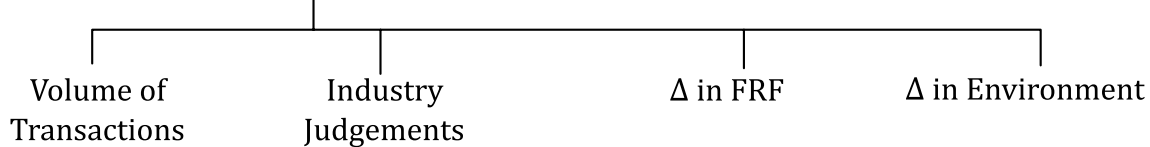


\* Factors to be considered → for establishing Audit Strategy

(1) Identify → Characteristic → of Engagement



3. Consider → Significant Factors → in directing → Team's Efforts



4. Consider → Result — Preliminary Engagement Activities  
Relevant Knowledge of Engagement Partner

5. Ascertain → N.E.T. → of Resources Necessary

**The elements of planning can be categorized as under:**

- (i) Preliminary engagement activities
- (ii) Planning activities

**(1) Preliminary engagement activities**

The auditor considers whether relationship with client should be continued and whether ethical requirements including independence continue to be complied with. It includes:

- (A) Performing procedures regarding the continuance of the client relationship
- (B) Evaluating compliance with ethical requirements, including independence
- (C) Establishing an understanding of terms of engagement

**Preliminary engagement activities include the following:**

**(A) Performing procedures regarding the Continuance of Client Relationships and Audit Engagements:** Acceptance and Continuance of Client Relationships and Audit Engagements It should be ensured that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed and that conclusions reached in this regard are appropriate.

The firm should obtain information considered necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client.

Matters such as integrity of principal owners and key management, competence of engagement team to perform the audit engagement and implications of matters that have arisen during current and previous audit engagement may need to be considered. Besides, in case of initial engagements, communication with predecessor auditor should be made, where there has been a change of auditors.

**(B) Evaluating compliance with ethical requirements including independence:** The auditor shall continuously evaluate compliance with ethical requirements including independence. "Independence" means that the judgement of a person is not subordinate to the wishes or direction of another person who might have engaged him.

Throughout the audit engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team. If matters come to the engagement partner's attention that indicate that members of the engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action.

The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall:

- (i) Obtain relevant information from the firm to identify and evaluate circumstances and relationships that create threats to independence Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for the audit engagement and take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is permitted by law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action.

Besides, consideration for client continuance and compliance with ethical requirements, preliminary engagements activities also include establishing an understanding of terms of engagement.

- (C) **Establishing an understanding of terms of engagement:** It is in the interests of both the entity and the auditor that the auditor sends an audit engagement letter before the commencement of the audit to help avoid misunderstandings with respect to the audit. It ensures that there is no confusion with the client regarding terms of the engagement.

Performing preliminary engagement activities assists the auditor in identifying and evaluating events or circumstances that may affect auditor's ability to plan and perform audit engagement.

### **Planning activities**

**Planning activities involve:** Establishing the overall audit strategy Developing an audit plan

- (A) Establishing the overall audit strategy- Assistance for the auditor Overall audit strategy sets the scope, timing and direction of the audit, and guides the development of the more detailed audit plan.

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:

- (i) 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
- (ii) 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
- (iii) When these resources are to be deployed, such as whether at an interim audit stage or at key cut-off dates
- (iv) 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 (for example, on-site or off-site), and whether to complete engagement quality control reviews



Factors to be taken into consideration by auditor for establishing audit strategy The auditor shall take following factors into consideration while establishing audit strategy:

- (a) Identify the characteristics of the engagement that define its scope It is important for auditor to identify scope of the engagement. Only a well identified scope can lead to establishment of a sound audit strategy. There are many characteristics of engagement defining its scope. Some of characteristics are as under:
- Applicable financial reporting framework applicable to the entity
  - Nature of business segments to be audited including the need for specialized knowledge
  - Industry specific reporting requirements required by industry regulators
  - Expected use of audit evidence obtained in previous audits

- (b) Ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required.

The ascertaining of reporting objectives of engagement helps the auditor to plan timing of different audit procedures and also nature of communications. Some of the instances are given under: -

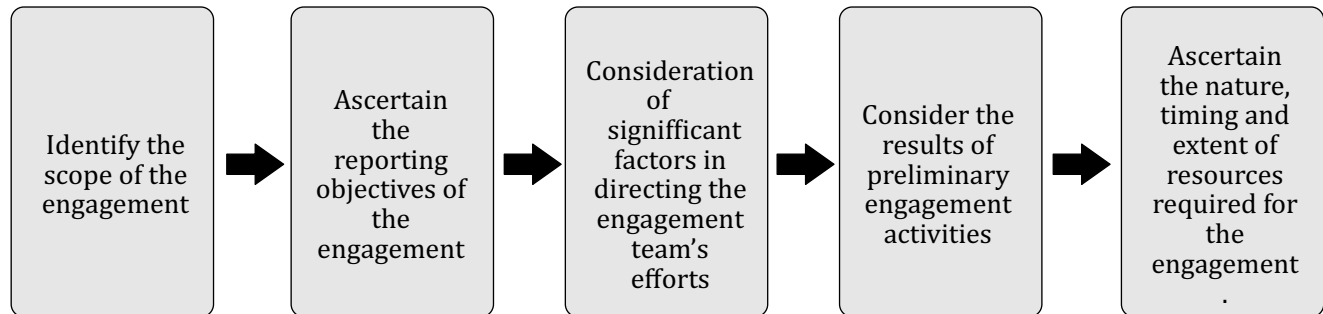
- The entity's timetable for reporting
  - Organization of meetings to discuss of nature, timing and extent of audit work with management
  - Discussion with management regarding the expected type and
  - timing of reports to be issued including the auditor's report
  - Discussion with management regarding the expected communications on the status of audit work throughout the engagement.
  - Expected nature and timing of communications among engagement team members, including the nature and timing of team meetings and timing of the review of work performed.
- (c) Consider the factors that, in the auditor's professional judgment, are significant in directing the engagement team's efforts

The auditor needs to direct efforts of engagement team towards matters that in his professional judgment are significant. Preliminary identification of material classes of transactions, account balances and disclosures help auditor in establishing overall audit strategy. More energies need to be devoted to significant matters to obtain desired outcomes. Few examples are listed as under:

- Volume of transactions which may determine whether it is more efficient for the auditor to rely on internal control
  - Significant industry developments such as changes in industry regulations and new reporting requirements.
  - Significant changes in the financial reporting framework, such as changes in accounting standards.
  - Other significant relevant developments, such as changes in the legal environment affecting the entity.
- (d) 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: Considering results of preliminary engagement activities and knowledge gained from similar engagements goes a long way in establishing sound audit strategy. Examples are listed as under:
- Results of previous audits that involved evaluating the operating effectiveness of internal control, including the nature of identified deficiencies and action taken to address them.

- The manner in which the auditor emphasizes to engagement team members the need to maintain a questioning mind and to exercise professional skepticism in gathering and evaluating audit evidence.
- (e) Ascertain the nature, timing and extent of resources necessary to perform the engagement. Selection of engagement team and assignment of audit work to team members is a significant factor in establishing overall audit strategy. Experienced team members may be assigned in areas where there is higher risk of material misstatement. Similarly, engagement budgeting and devotion of more time to areas of higher risk of material misstatement are to be kept in mind.

**In establishing the overall audit strategy, the auditor shall:**



## QUESTIONS

### Correct/Incorrect

**State with reasons (in short) whether the given statements are correct/incorrect:**

2. 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.

**Ans. (Incorrect)**

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.

3. Planning is a discrete phase of an audit.

**Ans. (Incorrect)**

Planning is not a discrete phase of an audit, but rather a continual and iterative process that often begin 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.

### Theory Questions

4. 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.

**Ans.** 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:

Helping the auditor to devote appropriate attention to important areas of the audit. Helping the auditor identify and resolve potential problems on a timely basis.

Helping the auditor properly organize and manage the audit engagement so that it is performed in an effective and efficient manner.

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.

Facilitating the direction and supervision of engagement team members and the review of their work. Assisting, where applicable, in coordination of work done by auditors of components and experts.

**Illustration 1:** The auditor T of Hand Fab Ltd is worried as to management of key resources to be employed to conduct audit.

### Required

How the audit strategy would be helpful to the auditor?

**Solution:** Refer-Establishing the overall audit strategy- Assistance for the auditor for solution.

### Development of 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.

Understanding client's business is one of the important principles in developing an audit plan. In fact, without adequate knowledge of client's business, a proper audit is not possible. Gaining knowledge of client's business is, therefore, one of the foremost requirements to develop audit plan.

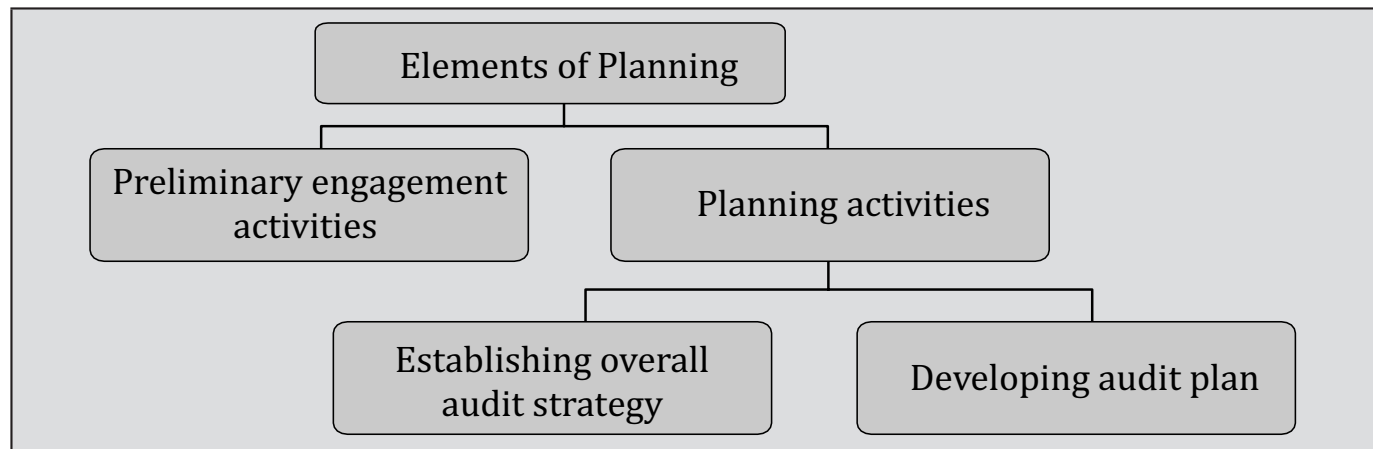
SA-300 states that auditor shall develop an audit plan that shall include description of-

- (i) The nature, timing and extent of planned risk assessment procedures
- (ii) The nature, timing and extent of planned further audit procedures at assertion level
- (iii) Other planned audit procedures that are required to be carried out so that the engagement complies with SAs.

The auditor plans what type of audit procedures are to be performed, their timing and how much work should be done taking into account sample size etc.

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.

For example, planning of the auditor's risk assessment procedures occurs early in the audit process. 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 further audit procedures.



### Test Your Understanding

1. MG & Co, a firm of auditors, having a standing of 30 years is appointed as a statutory auditor of company engaged in manufacturing of defence equipment. Due to opening of defence sector by government to private players in recent times, many new companies have entered the fray to manufacture sophisticated defence equipment. Considering technical and complex nature of operations, the auditors recognize that involvement of experts in the audit is required. Does consideration for involvement of experts by auditors fall in the domain of planning audit?

**Ans.** Consideration for involvement of experts by auditors falls within domain of planning. While planning an audit, auditor would have to consider whether involvement of experts is necessary. In the stated case, company is involved in technical and complex operations. Therefore, while planning an audit, auditors would have to consider whether involvement of expert is necessary.

2. CA Kartik is planning for audit of a company engaged in manufacturing of cosmetics. Considering nature of operations of the company, he had planned to include testing of controls of the company over purchases, sales and inventories. One fine day, he reaches the corporate office and asks for manuals and required documentation to ensure surprise element in testing. He had never shared with management his intention to carry out above procedures. Is approach of CA Kartik proper?

**Ans.** In the case, CA Kartik has reached office of the company without sharing with management his intention to test the controls. The auditor may decide to discuss elements of planning with the entity's management to facilitate the conduct and management of the audit engagement without compromising effectiveness of audit. Sharing details of visit to test controls does not.

### Multiple Choice Questions (MCQ)

2. Which of the following is true about audit plan?

Once an audit plan has been finalized for an engagement,

- (a) changes cannot be made to it Audit plan includes scope, timing and direction of planned
- (b) assessment procedures
- (c) Changes in audit plan cannot lead to change in audit strategy
- (d) Audit plan has to be documented by auditor

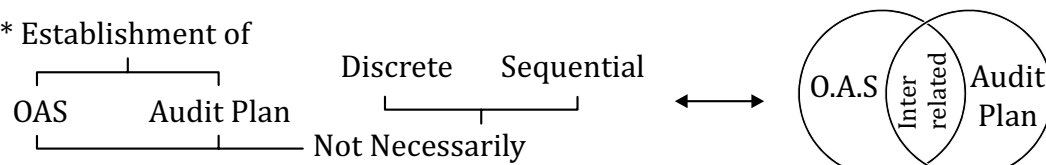
**Ans.** (d) Audit plan has to be documented by auditor



## ■ RELATION BETWEEN AUDIT STRATEGY & AUDIT PLAN

Audit Strategy	Audit Plan
Sets Broad Overall Approach	<input type="checkbox"/> Addresses Various Matters Identified in OAS
Determines $\left\{ \begin{array}{l} S \\ T \\ D \end{array} \right.$ of Audit	<input type="checkbox"/> Describes How Strategy is going to be implemented
Less Detailed than Audit plan	<input type="checkbox"/> More Detailed than OA's <input type="checkbox"/> Includes Net of Audit Procedures
OAS is established First	<input type="checkbox"/> Audit plan can be developed After OAS

\* Establishment of



Audit strategy sets the broad overall approach to the audit whereas audit plan addresses the various matters identified in the overall audit strategy. Audit strategy determines scope, timing and direction of audit. Audit plan describes how strategy is going to be implemented. 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.

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.

### QUESTIONS

#### Correct/Incorrect

State with reasons (in short) whether the following statements are correct or incorrect:

- 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.

#### Ans. (Correct)

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. The establishment of



## ■ OVERALL AUDIT STRATEGY AND THE AUDIT PLAN-THE AUDITOR'S RESPONSIBILITY

Responsibility → Remains with Auditor



May Discuss



Elements of Planning



Without Compromising Effectiveness of Audit

The overall audit strategy and the audit plan remain the auditor's responsibility. It is the auditor who is responsible for establishing overall audit strategy and developing audit plan. However, as discussed earlier, auditor may discuss elements of planning with entity's management without compromising effectiveness of audit.

**Illustration 2:** W, the auditor of SKM Ltd. asks its finance and audit head to prepare audit strategy for conducting audit of SKM Ltd. W also insists him to draw detailed audit procedures. On the request of auditor W completes audit strategy as well as audit procedures as prepared by finance head of the company. Subsequently, auditor realizes that effectiveness of the audit is compromised and it was his responsibility to prepare the overall audit strategy. Comment.

**Solution:** Refer - Overall audit strategy and the audit plan- The auditor's responsibility - Accordingly, approach of W was wrong and he should have prepared overall audit strategy and detailed audit procedures.

### Notes to Add

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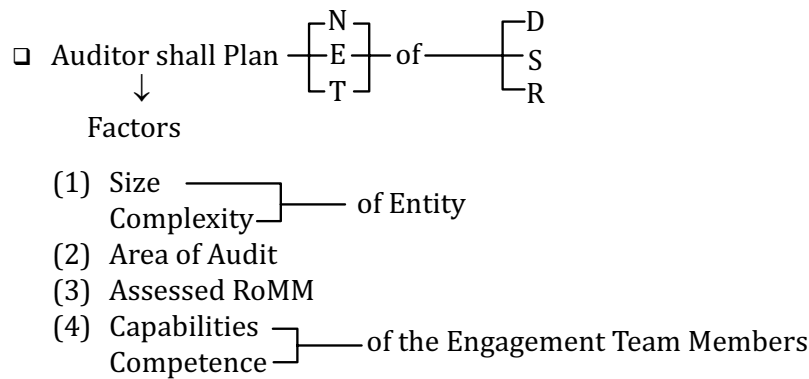
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## ■ PLANNING SUPERVISION AND REVIEW OF WORK OF ENGAGEMENT TEAM MEMBERS



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.

### QUESTIONS

#### Theory Questions

**10.** SA 300 states that auditor shall plan the nature, timing and extent of direction and supervision of engagement team members and the review of their work. Discuss few factors affecting such supervision and review of work of engagement team members.

**Ans.** Points on Planning supervision and review of work of engagement team members.

- (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.

#### Notes to Add

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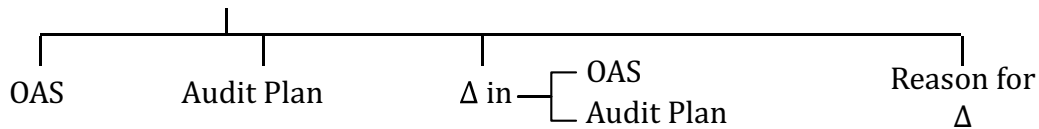
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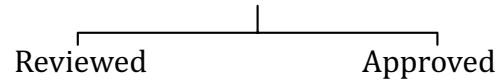
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## ■ DOCUMENTATION



□ Documentation = Record of : -

- (i) RAP & FAP
- (ii) Proper Planning of Audit Procedures



□ Auditor May Use → STANDARD — Audit Program  
— Audit Completion Check List

→ Tailored → as needed

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.

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.

### Test Your Understanding

3. CA Mary, while planning audit of a company, feels that she would inquire from inhouse legal counsel of the company status of pending litigation matters against the company to identify and assess risks of material misstatements. Considering above description, are you able to identify said procedures? Where these identified procedures are included in planning in accordance with SA-300?

**Ans.** These are planned risk assessment procedures to identify and assess risk of material misstatement. The objective of planned inquiry of inhouse legal counsel is to identify and assess risk of material misstatement. Such planned risk assessment procedures are included in audit plan in accordance with SA-300.

4. CA Shubhendu is statutory auditor of a social media company. Due to change in information technology regulations by government, it has become mandatory for such companies to constitute “grievance redressal mechanism” for users of social media platform of the company. Failure to comply with regulations can potentially lead to civil and criminal liabilities against the company. Is above factor to be considered by auditor while framing audit strategy?

**Ans.** Changes in laws and regulations affecting the company is a factor to be considered while establishing overall audit strategy. There has been change in information technology regulations applicable to the company. Non-compliance of the same can have implications in form of civil and criminal liabilities. Such an important matter concerning changes in laws and regulations is to be considered

## QUESTIONS

### Theory Questions

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

**Ans.** 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.

12. An auditor of a company fails to document audit strategy and audit plan. Briefly outline consequences of such failure.

**Ans.** 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.

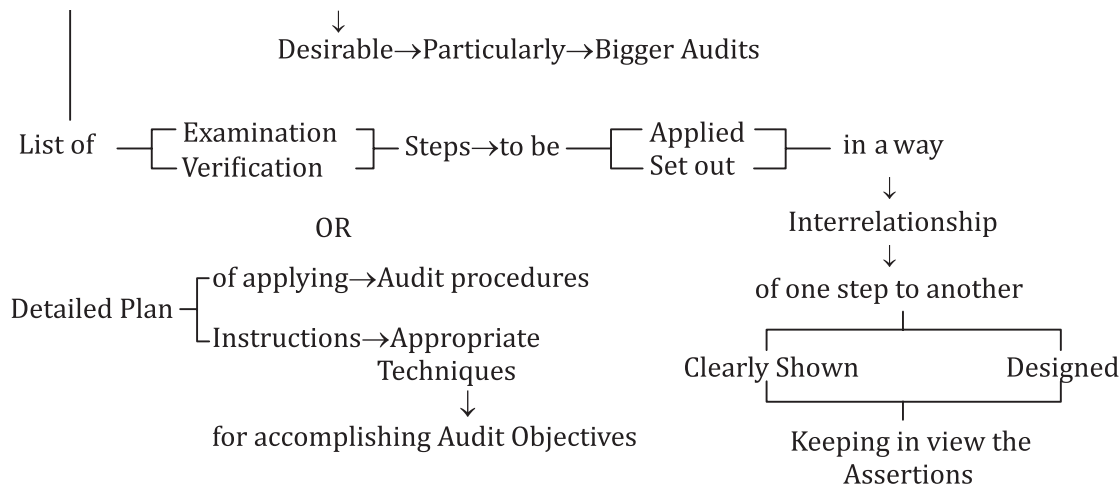
A record of the significant changes to the overall audit strategy and the audit plan, and resulting changes to the planned nature, timing and extent of audit procedures, explains why the significant changes were made, and the overall strategy and audit plan finally adopted for the audit. It also reflects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

### Notes to Add

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## ■ AUDIT PROGRAMME



It is desirable that in respect of each audit and more particularly for bigger audits, an audit programme should be drawn up. Audit programme is a list of examination and verification steps to be applied and set out in such a way that the interrelationship 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.

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

In other words, an audit programme 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.

## QUESTIONS

### Multiple choice Questions (MCQ)

4. Which of the following is not included in an audit programme normally?

- (a) Extent of checking
- (b) Date of checking
- (c) Nature or type of procedure
- (d) Planning of risk assessment procedures

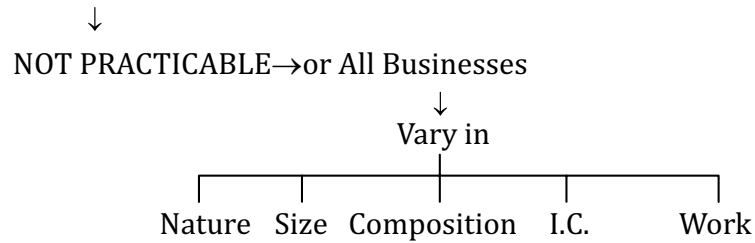
**Ans.** (d) Planning of risk assessment procedures

### Theory Questions

13. "Purported disadvantages of an audit programme can be overcome". Do you agree?

**Ans.** Purported disadvantages of audit programme 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.

## ■ EVOLVING ONE AUDIT PROGRAMME-NOT PRACTICABLE FOR ALL BUSINESSES



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. 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.

### QUESTIONS

#### Correct/Incorrect

State with reasons (in short) whether the following statements are correct or incorrect:

14. A detailed Audit Programme once prepared for a business can be used for all business under all circumstances.

**Ans. (Incorrect)**

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.

#### Notes to Add

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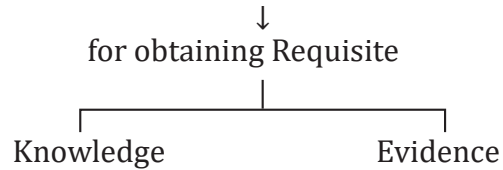
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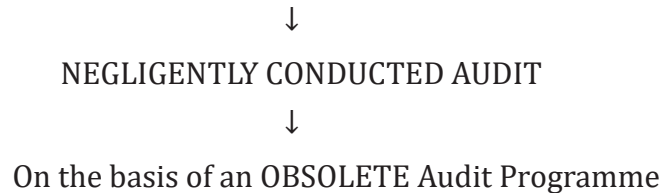


## ■ PERIODIC REVIEW OF AUDIT PROGRAMME

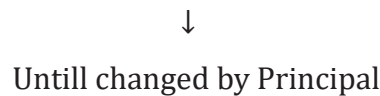
- To Assess → Whether → Same continues to be ADEQUATE



- Auditor → may have to face legal consequences



- Audit Assistants → Unfailingly → Follow Instructions of Audit Programme



If periodic review is conducted → it removes RIGIDITY

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.

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. 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. 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.

### **Notes to Add**

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## ■ CONSTRUCTING AN AUDIT PROGRAMME

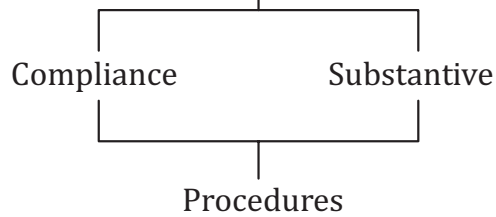
- Audit Planning Related Program } Commences → Conclusion → P.Y. Audit



Reconsidered → for Modification

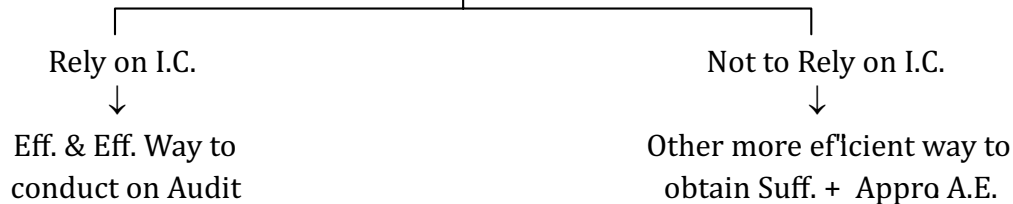


- Based on {
  - Review of I.C.
  - Preliminary Evaluation
  - Result of

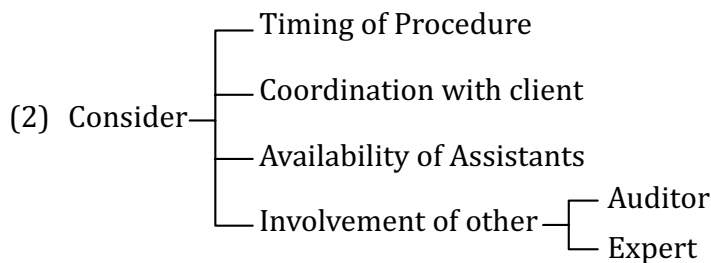


- While developing Audit Program → Auditor MAY

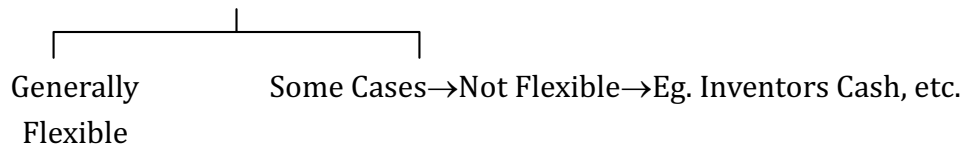
(1)



(2)



(3) When to Perform Audit Procedure



- Construction of Audit Programme:

(1) Stay within [ Scope / Limitation ] of the assignment

(2) Prepare → Written Audit Programme

(3) Identify → Best Evidence

- (4) Apply → Only useful steps
- (5) Include → Audit Objectives → of each area
- (6) Consider → Possibilities of Errors
- (7) Co-Ordinate → Procedures

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.

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.

Further, 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.

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

- (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.

## QUESTIONS

### Correct/Incorrect

**State with reasons (in short) whether the following statements are correct or incorrect:**

- 15.** A detailed Audit Programme once prepared for a business can be used for all business under all circumstances.

**Ans. Incorrect:** 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.

16. Materiality is not a matter of size.

**Ans. Incorrect:** 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.

### Theory Questions

17. "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.

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

- (a) It provides the assistant carrying out the audit with total and clear set of instructions of the work generally to be done.
- (b) It is essential, particularly for major audits, to provide a total perspective of the work to be performed.
- (c) Selection of assistants for the jobs on the basis of capability becomes easier when the work is rationally planned, defined and segregated.
- (d) 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, such danger is significantly less and the audit can proceed systematically.
- (e) 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.
- (f) 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.
- (g) It serves as a guide for audits to be carried out in the succeeding year.
- (h) 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.

18. M/s TP & 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.

**Ans.** The Assistant Engaged – Be Encouraged to Keep an Open Mind: 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. 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.

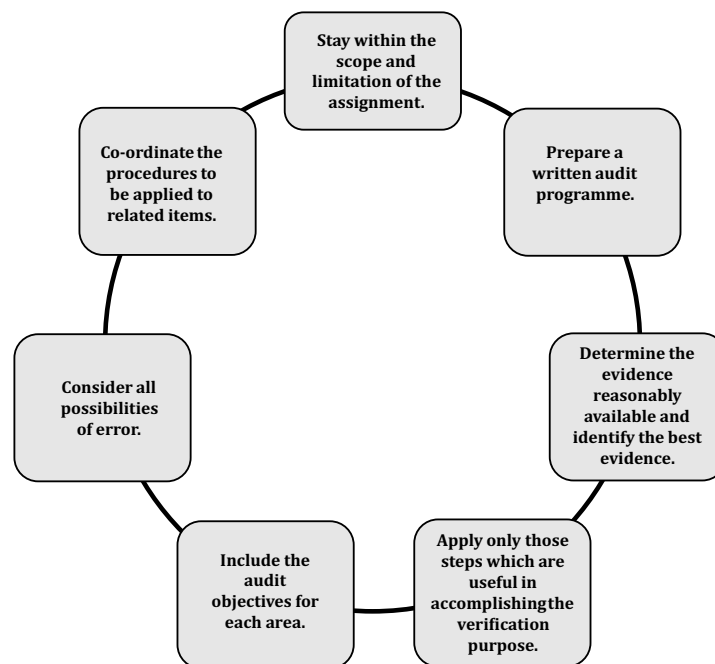
The assistant engaged in the job should be encouraged to keep an open mind beyond the programme given to him. He should be instructed to note and report significant matters coming to his notice, to his seniors or to the partners or proprietor of the firm engaged for doing the audit. In the given case, the attitude of assistants of TP & 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.

**19.** 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.

**Ans.** 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

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

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



## ■ AUDIT PROGRAMME - DESIGNED TO PROVIDE AUDIT EVIDENCE

- A.E. = INFO → used by Auditor → in Arriving @ Conclusion
  - ↓
  - Info. In Includes
  - ↓
  - On which Auditor's Opinion is based — { A/c. Records  
Other Info.
  
- A.E. → basis for formulation → of opinion
  - ↓
  - Audit Programme — { Procedures  
Techniques
  
- Assertions → Evidence is — { Drawn  
Considered  
Weighted
  - ↓
  - to
  - Prove Disprove

Audit evidence may be defined as the information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information.

Evidence is the very basis for formulation of opinion and an audit programme is designed to provide for that by prescribing procedures and techniques. What is best evidence for testing the accuracy of any assertion is a matter of expert knowledge and experience. 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. 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:

- (a) Documentary examination
- (b) Physical examination
- (c) Statements and explanation of management, officials and employees
- (d) Statements and explanations of third parties
- (e) Arithmetical calculations by the auditor
- (f) State of internal controls and internal checks
- (g) Inter-relationship of the various accounting data
- (h) Subsidiary and memorandum records
- (i) Minutes
- (j) 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.

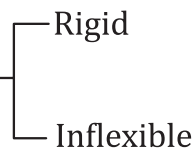


## ■ ADVANTAGES & DISADVANTAGES OF AUDIT PROGRAMME

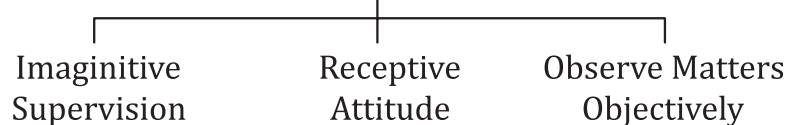
### Advantages

- (1) Total + Clear → Set of Instructions
- (2) Provide → Perspective → of work to be performed
- (3) Selection of capable assistants
- (4) Audit can proceed systematically
- (5) Work may be tracked back to the assistant
- (6) Principal can track progress
- (7) Serves as a guide for future Auditors
- (8) Serves as evidences

### Disadvantages

- (1) Work → may become → mechanical
  - (2) Programme → tends to become
  - (3) Inefficient assistants → may take shelter
  - (4) Hard & Fast Audit Programme → may kill initiative
- 

### Disadvantages may be overcome by



### The advantages of an audit programme are:

- (a) It provides the assistant carrying out the audit with total and clear set of instructions of the work generally to be done.
- (b) It is essential, particularly for major audits, to provide a total perspective of the work to be performed.
- (c) Selection of assistants for the jobs on the basis of capability becomes easier when the work is rationally planned, defined and segregated.
- (d) 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, such danger is significantly less and the audit can proceed systematically.
- (e) 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.
- (f) 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.
- (g) It serves as a guide for audits to be carried out in the succeeding year.
- (h) 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.



Some disadvantages are also there in the use of audit programmes but most of these can be removed by following some concrete steps.

**The disadvantages are:**

- (a) 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.
- (b) 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.
- (c) 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.
- (d) A hard and fast audit programme may kill the initiative of efficient and enterprising assistants.

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.

## QUESTIONS

### Multiple Choice Questions (MCQ)

5. Which of the following is not an advantage of an audit programme?

- (a) It acts as a guide for audit of coming years.
- (b) It fixes responsibility of assistants.
- (c) It serves as a shelter for assistants.
- (d) It serves a proof of work done by auditor.

**Ans.** (c) It serves as a shelter for assistants.

### Test Your Understanding

5. Rohit, undergoing practical training, is part of an engagement team conducting audit of a company engaged in manufacturing of paints. He has been provided with audit programme pertaining to sales. It lists out various items to be checked and verified by him including invoices, rate lists, posting in debtors accounts, correlation of invoices with e-way bills on sample basis etc. During verification, he notices that many e-way bills have been cancelled by the company within 24 hours of their generation in month of March. There is no specific instruction in audit programme in this regard. He keeps mum. Is attitude of Rohit proper?

**Ans.** Attitude of Rohit is not proper. The assistants should observe matters objectively and bring significant matters to the notice of supervisor/principal. Reasons for cancellation of many e-way bills in month of March need to be looked into. Matter should be informed to engagement partner.





## QUESTIONS

### Multiple choice Questions (MCQ)

#### Based on above, answer following questions

6. Auditor is fact checking about promoters and key managerial persons. She is also considering competence of staff to perform engagement. What is she trying to do?

- (a) She is establishing audit strategy
- (b) She is conducting preliminary engagement activities
- (c) She is designing audit plan
- (d) She is checking her compliance of ethical requirements

**Ans.** (b) She is conducting preliminary engagement activities

7. Consideration of number and location of branches, requirements of financial reporting framework and expected time of completion are relevant factors primarily for which of the following -

- (a) Developing audit plan
- (b) Establishing overall audit strategy
- (c) Designing audit programme
- (d) Designing risk assessment procedures

**Ans.** (b) Establishing overall audit strategy

8. Taking into account description of planned inquiry and visit, which of the following statements is TRUE?

- (a) Planned inquiry and visit fall in area of audit strategy
- (b) Planned inquiry and visit are planned risk assessment procedures and fall in field of audit plan
- (c) The said description is not related to audit planning
- (d) Planned inquiry and visit fall in scope of audit programme

**Ans.** (b) Planned inquiry and visit are planned risk assessment procedures and fall in field of audit plan

9. What is detailed set of instructions given to assistants in engagement team known as?

- (a) Audit guidelines
- (b) Audit plan
- (c) Audit Programme
- (d) Audit Procedures

**Ans.** (c) Audit Programme

10. The issue of generation of scrap has been overlooked in detailed set of instructions given to engagement team. What should be proper course of action by CA Simran Kaur?

- (a) She should ignore this information as audit has already begun
- (b) She should modify earlier set of instructions
- (c) She should leave the matter to wisdom of engagement team
- (d) She should put the ball in court of management as she was not provided with complete information earlier

**Ans.** (b) She should modify earlier set of instructions

