

**SA 500 - Audit Evidence**

<p><b>Sufficiency (Quantity) &amp; Appropriateness (Quality) of audit evidence</b></p> <p>Auditor's judgement as to <b>sufficiency</b> may be <b>affected by factors</b> such as -</p> <ul style="list-style-type: none"> <li>• <b>Materiality</b> - <b>Less evidence</b> would be required in case assertions are <b>less material</b> to users of FS</li> <li>• <b>ROMM</b> - <b>Less evidence</b> would be required in case assertions that have a <b>lower ROMM</b></li> <li>• <b>Size &amp; characteristics of population</b> - <b>Less evidence</b> would be required in case of <b>smaller, more homogeneous</b> population</li> <li>• And <b>vice versa</b> for all</li> </ul>	<p><b>Appropriateness - Relevance and Reliability of audit evidence</b></p> <p>While there may be exceptions, following are <b>generalisations about reliability</b> of audit evidence, reliability of audit evidence <b>increases when</b> -</p> <ul style="list-style-type: none"> <li>• It is obtained from <b>independent sources</b> outside entity</li> <li>• Generated <b>internally</b>, related <b>controls</b> imposed by entity <b>are effective</b></li> <li>• It is obtained <b>directly by auditor</b> rather than evidence obtained indirectly</li> <li>• It is in <b>documentary form</b>, whether paper or electronic rather than evidence obtained orally</li> <li>• It is obtained as <b>original docs</b> rather than evidence obtained as photocopies</li> </ul>
<p><b>Audit procedures to obtain audit evidence include</b></p> <ul style="list-style-type: none"> <li>• <b>Inquiry</b> - It consists of seeking info of knowledgeable persons. Although inquiry may provide important audit evidence, inquiry <b>alone does not provide SAAE</b> of <b>absence of MM</b> at assertion level, nor of <b>operating effectiveness</b> of controls</li> <li>• <b>Analytical Procedures</b> - SA 520</li> <li>• <b>Observation</b> - It consists of <b>looking at process</b> being performed by others</li> <li>• <b>Reperformance</b> - It involves auditor's <b>independent execution of procedures</b> that were originally performed as part of entity's IC</li> <li>• <b>Inspection</b> - It involves <b>examining docs</b> in detail for obtaining evidence</li> <li>• <b>Recalculation</b> - It consists of <b>checking mathematical accuracy</b> of docs or records</li> <li>• <b>External Confirmation</b> - SA 505</li> </ul>	<p><b>Mgt Expert</b></p> <p>Individual or organisation possessing <b>expertise in field other than a/c or auditing</b>, whose work is used by entity in preparing FS</p> <p><b>When info to be used as audit evidence has been prepared using work of Mgt's Expert &amp; having regard to significance of expert's work for auditor's purposes, Auditor shall</b></p> <ul style="list-style-type: none"> <li>• Evaluate <b>competence, capabilities &amp; objectivity</b> of that expert</li> <li>• Obtain <b>understanding of work</b> of that expert</li> <li>• Evaluate <b>appropriateness</b> of that <b>expert's work</b> as audit evidence</li> </ul>

**Inconsistency in or Doubts over Reliability of Audit Evidence**

If Auditor finds any inconsistency in audit evidence or have doubts over their reliability, he shall

- Consider **effect** of matter
- **Modify** audit **procedures**

Inventory	Litigation and Claims
<p><b>When inventory is material to FS, auditor shall obtain SAAE regarding existence &amp; condition of inventory by</b></p> <ul style="list-style-type: none"> <li>• <b>Attendance</b> at physical inventory <b>counting</b>, unless impracticable, to –                             <ul style="list-style-type: none"> <li>○ <b>Evaluate Mgt’s instructions</b> &amp; procedures for recording results of physical inventory counting like –                                     <ul style="list-style-type: none"> <li>▪ Procedures used to <b>estimate physical quantities</b></li> <li>▪ Existence of appropriate <b>control activities</b></li> <li>▪ <b>Control over movement of inventory</b> b/w areas &amp; shipping &amp; receipt of inventory before &amp; after cut-off date</li> <li>▪ Accurate <b>identification of stage of completion</b> of WIP of slow moving, obsolete or damaged</li> </ul> </li> <li>○ <b>Observe performance</b> of Mgt’s count procedures</li> <li>○ <b>Perform test counts</b> to obtain SAAE –                                     <ul style="list-style-type: none"> <li>▪ <b>By tracing items</b> selected from physical inventory to Mgt’s count records</li> <li>▪ By obtaining <b>copies of Mgt’s completed</b> physical inventory count <b>records</b></li> </ul> </li> <li>○ <b>Inspect inventory</b> to identify obsolete/damaged</li> </ul> </li> <li>• Performing audit procedures over entity’s <b>final inventory records</b> to determine whether they <b>accurately reflect actual inventory count results</b></li> </ul> <p><b>Physical Inventory Counting Conducted other than at Date of FS</b></p> <ul style="list-style-type: none"> <li>• If auditor is <b>unable to attend</b> inventory counting due to <b>unforeseen circumstances</b>, Auditor shall observe count on <b>alternative date</b></li> <li>• Auditor shall perform audit procedures to obtain audit evidence about whether <b>changes in inventory</b> b/w count date and date of FS are <b>properly recorded</b></li> </ul> <p><b>Attendance at Physical Inventory Counting becomes impractical</b></p> <ul style="list-style-type: none"> <li>• This may be due to factors such as nature and location of inventory</li> <li>• Auditor shall perform <b>alternative audit procedures</b> to <b>obtain SAAE</b> regarding existence and condition of inventory</li> <li>• If it is <b>not possible</b> to do so, auditor shall <b>modify opinion</b></li> <li>• Matter of <b>general inconvenience</b> to auditor is <b>not a valid reason</b> for decision by auditor that attendance is impracticable</li> </ul>	<p><b>Auditor shall design &amp; perform audit procedures in order to identify litigation &amp; claims involving entity by</b></p> <ul style="list-style-type: none"> <li>• <b>Inquiry of Mgt</b> &amp; in- house legal counsel</li> <li>• <b>Reviewing minutes of meetings</b> of TCWG &amp; correspondence B/w entity &amp; external legal counsel</li> <li>• Reviewing <b>legal expense account</b></li> </ul> <p><b>Communication with Entity’s External Legal Counsel</b></p> <ul style="list-style-type: none"> <li>• If Auditor <b>assesses ROMM</b> regarding Litigation or Claims or</li> <li>• Co. has <b>not disclosed all</b> material litigation cases</li> <li>• Auditor shall <b>communicate</b> through <b>letter of inquiry prepared by Mgt &amp; sent by auditor</b> requesting entity’s <b>external legal counsel</b> to communicate directly with auditor</li> <li>• If <b>L&amp;R</b> or legal professional body <b>prohibits</b> entity’s external legal counsel <b>from communicating</b> directly with auditor, auditor shall <b>perform alternative audit procedures</b></li> <li>• If it is unlikely that external legal counsel will respond appropriately to letter of general inquiry, auditor may seek <b>direct communication through letter of specific inquiry</b>. Letter of specific inquiry <b>includes</b> –                             <ul style="list-style-type: none"> <li>• A <b>list of litigation</b> &amp; claims</li> <li>• <b>Mgt’s assessment of outcome</b> of each litigation &amp; claims &amp; its estimate of financial implications</li> <li>• A request that entity’s external legal counsel <b>confirm reasonableness of mgt’s assessments</b> &amp; provide info if list is incomplete or incorrect</li> </ul> </li> </ul> <p><b>Meeting with Entity’s External Legal Counsel</b></p> <ul style="list-style-type: none"> <li>• In certain circumstances, auditor may judge it necessary to meet with entity’s external legal counsel to <b>discuss likely outcome of litigation</b> or claims. This may be case, for e.g. where –                             <ul style="list-style-type: none"> <li>○ Matter is <b>complex</b></li> <li>○ Matter is a <b>significant risk</b></li> <li>○ There is <b>disagreement</b> b/w <b>mgt</b> &amp; entity’s external <b>legal counsel</b></li> </ul> </li> <li>• Such meetings require <b>mgt’s permission</b> and are held with <b>representative of mgt</b> in attendance</li> <li>• Further if –                             <ul style="list-style-type: none"> <li>○ <b>Mgt refuses</b> to give auditor <b>permission</b> to communicate <b>or meet</b> with entity’s external legal counsel or</li> <li>○ Entity’s external <b>legal counsel refuses to respond</b> appropriately to letter of inquiry, <b>or is prohibited</b> from responding &amp;</li> </ul> </li> </ul>

<ul style="list-style-type: none"> <li>• Matter of <b>difficulty, time or cost</b> involved is <b>not</b> itself a <b>valid basis</b> for auditor to <b>omit</b> an audit <b>procedure</b> for which there is <b>no alternative</b> or to be satisfied with audit evidence that is <b>less than persuasive</b></li> </ul> <p><b>When inventory under custody and control of third party</b></p> <p>If inventory is <b>material to FS</b>, auditor shall -</p> <ul style="list-style-type: none"> <li>• <b>Request confirmation</b> from third party as to quantities and condition of inventory held on behalf of entity</li> <li>• <b>Perform inspection</b> or other procedures as appropriate in circumstances</li> </ul> <p>If <b>doubt</b> is raised about <b>integrity &amp; objectivity of 3<sup>rd</sup> party</b>, Auditor may perform following audit procedures -</p> <ul style="list-style-type: none"> <li>• <b>Requesting confirmation</b> from other parties when inventory has been <b>pledged as collateral</b></li> <li>• <b>Inspecting documentation</b> regarding inventory held by 3<sup>rd</sup> parties</li> <li>• <b>Attending</b>, or arranging for <b>another auditor</b> to attend, <b>3<sup>rd</sup> party's physical counting</b> of inventory</li> <li>• Obtaining another auditor's <b>report on adequacy of 3<sup>rd</sup> party's IC</b> for inventory</li> </ul>	<ul style="list-style-type: none"> <li>○ Auditor is <b>unable to obtain SAAE</b> by performing <b>alternative</b> audit procedures</li> <li>○ Auditor shall <b>modify opinion</b> in auditor's report as per SA 705</li> </ul> <p><b>Written representation from Mgt &amp; TCWG</b></p> <ul style="list-style-type: none"> <li>• <b>All known actual or possible</b> litigation &amp; claims whose effects should be considered when preparing FS have been <b>disclosed to auditor &amp;</b></li> <li>• Appropriately <b>accounted for &amp; disclosed</b> as per AFRF</li> </ul>
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**Segment Information**

Auditor shall obtain SAAE regarding **presentation & disclosure** of segment info as per AFRF by -

- Obtaining **understanding of methods used by Mgt** in determining segment info, and –
  - Evaluating whether such methods are likely to result in **disclosure as per AFRF**
  - Where appropriate, **testing application** of such methods
  - **Eg of matters** relevant when obtaining above understanding include –
    - **Sales, transfers & charges** b/w segments, & elimination of inter segment amounts
    - **Comparisons with budgets** & expected results
    - **Consistency with prior periods**, & adequacy of disclosures for inconsistencies
    - **Allocation of assets** & costs among segments
- **Performing AP** or other procedures appropriate in circumstances

Audit Evidence obtained as **Direct Written Response** to Auditor from a **3<sup>rd</sup> Party**

<p><b>Positive confirmation request</b></p> <ul style="list-style-type: none"> <li>• A request that confirming party respond directly to auditor indicating <b>whether confirming party agrees or disagrees</b> with info in request, or <b>providing requested info</b></li> <li>• A response to positive confirmation request is expected to <b>provide reliable audit evidence</b></li> <li>• However, there is a <b>risk</b> that confirming party may reply to confirmation request <b>without verifying that info is correct</b></li> <li>• Auditor may <b>reduce</b> this risk by <b>not stating amount</b> on confirmation request, &amp; ask confirming party to fill in amount</li> <li>• However, it may result in <b>lower response rates</b> because <b>additional effort</b> is required by confirming parties</li> </ul> <p><b>Non-response</b></p> <p>A <b>failure</b> of confirming party <b>to respond</b>, to a positive confirmation request, or a confirmation request <b>returned undelivered</b></p> <p><b>Exception</b></p> <p>Response that indicates a <b>diff b/w info requested</b> to be confirmed and <b>info provided</b> by confirming party</p>	<p><b>Negative confirmation request</b></p> <ul style="list-style-type: none"> <li>• A request that confirming party respond directly to auditor <b>only if confirming party disagrees</b> with info provided in request</li> <li>• They provide <b>less persuasive audit evidence</b> than positive confirmations</li> <li>• <b>Failure to receive response</b> to negative confirmation request does <b>not</b> explicitly indicate <b>receipt by intended confirming party</b> of confirmation request or <b>verification</b> of accuracy of info contained in request</li> <li>• Confirming parties also may be <b>more likely to respond</b> indicating their disagreement with a confirmation request when info in request is <b>not in their favour</b>, and less likely to respond otherwise</li> <li>• Accordingly, auditor shall <b>not use</b> negative confirmation requests <b>as sole substantive audit procedure</b> to address an assessed ROMM <b>unless ALL</b> of following are <b>present</b> – <ul style="list-style-type: none"> <li>○ Auditor has assessed <b>ROMM as low</b> and has obtained <b>SAAE regarding operating effectiveness</b> of controls</li> <li>○ A <b>very low exception rate</b> is expected</li> <li>○ Population comprises a large number of <b>small &amp; homogeneous items</b></li> <li>○ Auditor is <b>not aware of circumstances</b> that would cause recipients of negative confirmation to <b>disregard such requests</b></li> </ul> </li> </ul>
<p><b>Mgt’s refusal to allow auditor to send confirmation request</b></p> <p>If mgt refuses to allow auditor to send a confirmation request, auditor shall -</p> <ul style="list-style-type: none"> <li>• <b>Inquire as to mgt’s reasons</b> for refusal, and seek audit evidence as to their validity and reasonableness</li> <li>• <b>Evaluate implications</b> of mgt’s refusal on auditor’s <b>assessment of ROMM</b>, including risk of fraud</li> <li>• Perform <b>alternative audit procedures</b> designed to obtain relevant and reliable audit evidence</li> <li>• If auditor concludes that <b>mgt’s refusal</b> to allow auditor to send confirmation request is <b>unreasonable</b>, or</li> <li>• Auditor is <b>unable to obtain</b> relevant and reliable audit <b>evidence</b> from alternative audit procedures</li> <li>• Auditor shall <b>communicate with TCWG</b> as per SA 260</li> <li>• Auditor also shall determine <b>implications for auditor’s opinion</b> as per SA 705</li> </ul>	<p><b>Results of External Confirmation procedures</b></p> <ul style="list-style-type: none"> <li>• <b>Reliability of responses to confirmation requests</b> - If auditor has doubt about reliability of response, auditor to obtain <b>further audit evidence</b>. If auditor determines response is not reliable, auditor to evaluate <b>implications on assessment of ROMM Factors</b> that may <b>indicate doubts</b> about reliability <ul style="list-style-type: none"> <li>○ It was <b>received</b> by auditor <b>indirectly or</b></li> <li>○ It appears <b>not to come</b> from originally intended <b>confirming party</b></li> </ul> </li> <li>• <b>Non-Response</b> - Auditor shall perform <b>alternative audit procedures</b></li> <li>• <b>When a response to positive confirmation is necessary and same is not received</b> - Determine implications on audit and <b>auditor’s opinion</b></li> <li>• <b>Exception</b> - Auditor shall <b>investigate</b> exceptions to determine whether or not they are <b>indicative of misstatement</b></li> </ul>

Opening Balances include **FS amounts** & **disclosure** at beginning of period, such as contingencies and commitments

<p><b>Initial audit engagement</b></p> <p>It refers to engagement in which either -</p> <ul style="list-style-type: none"> <li>• FS for prior period were <b>not audited</b> or</li> <li>• FS for prior period were <b>audited by predecessor auditor</b></li> </ul> <p><b>Predecessor Auditor</b></p> <p>Auditor from a <b>diff audit firm</b>, who audited FS of entity in prior period</p> <p><b>Objective of Auditor with respect to Opening Balances</b></p> <p>In conducting initial audit engagement, objective of auditor is to <b>obtain SAAE</b> about whether -</p> <ul style="list-style-type: none"> <li>• <b>Opening balances</b> contain <b>misstatements</b> that <b>materially affect</b> current period's FS</li> <li>• Appropriate <b>A/c policies</b> reflected in opening balances have been <b>consistently applied</b> in current period's FS, or <b>changes</b> thereto are <b>accounted and disclosed</b> as per AFRF</li> </ul>	<p><b>Obtaining SAAE about opening balances by Auditor by</b></p> <ul style="list-style-type: none"> <li>• Determining whether opening balances reflect application of <b>appropriate A/c policies</b></li> <li>• Determining whether prior period's closing balances have been <b>correctly brought forward</b> to current period or any <b>adjustments have been disclosed</b> as prior period items in current year's P/L</li> <li>• Performing one or more of following –             <ul style="list-style-type: none"> <li>○ Where prior year FS were audited, <b>reading audited FS</b></li> <li>○ Evaluating whether <b>audit performed in current period</b> provide evidence about opening balances</li> <li>○ <b>Performing specific audit procedures</b> to obtain evidence regarding opening balances</li> <li>○ Eg Procedures for <b>Opening Inventory</b> –                 <ul style="list-style-type: none"> <li>▪ Observing current physical <b>inventory count</b> &amp; <b>reconciling</b> it to opening inventory quantities</li> <li>▪ Performing procedure on <b>gross profit &amp; cut-off</b></li> <li>▪ Performing <b>procedures on valuation</b> of opening inventory items</li> </ul> </li> </ul> </li> </ul>
<p><b>Prior Period FS audited by Predecessor Auditor</b></p> <ul style="list-style-type: none"> <li>• When FS for preceding period were audited by predecessor auditor, current auditor may be able to obtain SAAE regarding opening balances by <b>perusing copies of audited FS of prior period</b></li> <li>• Current auditor <b>can place reliance</b> on closing balances contained in FS for preceding period, <b>except</b> when during current period, <b>possibility of misstatements</b> in opening balances is indicated</li> </ul>	<p><b>Modification in Predecessor Auditor's Report</b></p> <ul style="list-style-type: none"> <li>• If there was Modification in Predecessor Auditor's Report, auditor shall <b>evaluate effect</b> of matter giving rise to modification <b>wrt current period's FS</b></li> <li>• If modification is <b>relevant &amp; material</b> to current period's FS, auditor shall <b>modify auditor's opinion</b> on current period's FS as per SA 705</li> </ul>
<p><b>Communication with Mgt &amp; TCWG</b></p> <ul style="list-style-type: none"> <li>• If auditor obtains audit evidence that <b>opening balances contain misstatements</b></li> <li>• Auditor shall perform <b>additional procedures</b> to determine effect on current period's FS.</li> <li>• If auditor concludes that such misstatements <b>exist in current period's FS</b>, auditor shall communicate misstatements with <b>Mgt &amp; TCWG</b></li> </ul>	<p><b>Consistency of A/c Policies relating to opening balances</b></p> <p>If auditor concludes that -</p> <ul style="list-style-type: none"> <li>• Current period's a/c policies are <b>not consistently applied</b> in opening balances as per AFRF</li> <li>• <b>Change in a/c policies</b> is <b>not properly accounted</b> or disclosed as per AFRF,</li> <li>• Auditor shall express a <b>qualified or adverse opinion</b> as per SA 705</li> </ul>
<p><b>Reporting by auditor with regard to opening balances</b></p> <ul style="list-style-type: none"> <li>• If auditor is <b>unable to obtain SAAE</b> regarding opening balances, auditor shall express a <b>qualified or disclaimer of opinion</b>, as per SA 705</li> <li>• If auditor concludes that opening balances contain a <b>misstatement that materially</b> affects current period's FS, and effect of misstatement is <b>not properly accounted</b> or not disclosed, auditor shall express a <b>qualified or adverse opinion</b> as per SA 705</li> </ul>	

AP means evaluations of financial info through **analysis of plausible (logical) relationships** among both financial and non-financial data

<p><b>AP used as Substantive Tests</b></p> <p>When designing &amp; performing AP as substantive procedures as per SA 330, auditor shall -</p> <ul style="list-style-type: none"> <li>• Determine <b>suitability of particular AP</b> taking a/c of ROMM &amp; TOD</li> <li>• <b>Evaluate reliability of data</b> from which auditor’s expectation is developed</li> <li>• <b>Develop expectation</b> of recorded amounts &amp; evaluate whether expectation is sufficiently precise to identify MM</li> <li>• Determine amount of any <b>diff</b> of recorded amounts from expected values that is <b>acceptable without further investigation</b></li> </ul>	<p><b>Suitability of Particular AP for Given Assertions</b></p> <ul style="list-style-type: none"> <li>• AP are generally more applicable to <b>large volumes of transactions</b> that tend to be predictable over time</li> <li>• It also depends upon auditor’s assessment of <b>how effective it will be in detecting MM</b></li> <li>• <b>Different</b> types of AP provide <b>different levels of assurance</b></li> <li>• It is also influenced by <b>nature of assertion</b> &amp; auditor’s assessment of <b>ROMM</b></li> <li>• Particular AP may also be considered suitable when TODs are performed on same assertion</li> </ul>
<p><b>Reliability of Data</b></p> <p>When determining whether data is reliable for purposes of designing AP, <b>Factor determining extent of reliance</b> are -</p> <ul style="list-style-type: none"> <li>• <b>Nature &amp; relevance</b> of info available</li> <li>• <b>Source of info</b> available. For e.g., more reliable when obtained from independent sources</li> <li>• <b>Controls over preparation</b> of info that are designed to ensure its completeness, accuracy &amp; validity</li> <li>• <b>Comparability</b> of info available</li> </ul>	<p><b>Investigating results of AP</b></p> <p>If AP identify fluctuations or relationships that are <b>inconsistent</b> with other info or that <b>differ from expected values by a significant amount</b>, auditor shall investigate such differences by -</p> <ul style="list-style-type: none"> <li>• <b>Inquiring of mgt</b> &amp; obtaining appropriate audit <b>evidence relevant to mgt’s responses</b></li> <li>• <b>Performing other audit procedures</b> as necessary in circumstances –             <ul style="list-style-type: none"> <li>○ When mgt is <b>unable</b> to provide <b>explanation</b> or</li> <li>○ Explanation, together with audit evidence obtained relevant to Mgt’s response, is <b>not considered adequate</b></li> </ul> </li> </ul>

**Audit Sampling** - It refers to application of audit **procedures to less than 100%** of items within a population such that all sampling units have an **equal chance of selection** to provide reasonable basis for conclusion about entire population

**Tolerable misstatement** – Monetary amount set by auditor in respect of which auditor seeks to obtain appropriate level of **assurance that monetary amount is not exceeded by actual misstatement** in population

**Tolerable rate of deviation** – Rate of deviation from prescribed IC set by auditor in respect of which auditor seeks to obtain appropriate level of **assurance that it is not exceeded by actual rate of deviation** in population

**Anomaly** is **misstatement or deviation** that is **not representative** of misstatements or deviations in **population**

<p><b>Approaches to Sampling (Types of Sampling)</b></p> <ul style="list-style-type: none"> <li>• <b>Statistical sampling</b> is approach to sampling that has <b>random selection</b> of sample units; and use of <b>probability theory</b> to evaluate sample results.</li> <li>• In <b>larger</b> organisations, with huge transactions, statistical sampling is always recommended as it is <b>unbiased</b>, and samples selected are <b>not prejudged</b></li> <li>• <b>Non-Statistical Sampling</b> - Sampling on the basis of <b>personal experience and knowledge</b> of auditor</li> </ul> <p><b>Sample must be representative</b></p> <ul style="list-style-type: none"> <li>• Whatever is the approach, non-statistical or statistical, sample must be representative</li> <li>• This means that it <b>must be closely similar to whole population</b> although not necessarily exactly same</li> </ul>	<p><b>Types of Risks in Sampling</b></p> <ul style="list-style-type: none"> <li>• <b>Sampling risk</b> - is risk that <b>auditor's conclusion based on sample may be diff from conclusion if entire population</b> were subjected to same audit procedure.</li> <li>• It means that <b>sample was not representative</b> of population. It leads to 2 types of <b>erroneous conclusions</b> –             <ul style="list-style-type: none"> <li>○ In case of TOC, that controls are <b>more effective</b> than they actually are, or in case of TOD, that <b>MM does not exists</b> when in fact it does</li> <li>○ Auditor is concerned with this type of erroneous conclusion because it <b>affects audit effectiveness</b> &amp; is more likely to lead to <b>inappropriate audit opinion</b></li> <li>○ In case of TOC, controls are <b>less effective</b> than they actually are, or in case of TOD, that <b>MM exists</b> when in fact it does not</li> <li>○ This type of erroneous conclusion <b>affects audit efficiency</b> as it would usually lead to <b>additional work</b> to establish that initial conclusions were incorrect</li> </ul> </li> <li>• <b>Non-sampling risk</b> - is risk that auditor reaches an <b>erroneous (wrong) conclusion</b> for any <b>reason not related to sampling risk</b></li> </ul>
<p><b>Sample Size</b></p> <p>Auditor shall determine sample size sufficient <b>to reduce sampling risk to an acceptably low level</b>. The <b>lower the risk</b> the auditor is <b>willing to accept</b>, the <b>greater the sample size</b> will need to be</p> <p><b>Eg of Factors Influencing Sample Size –</b></p> <ul style="list-style-type: none"> <li>• <b>Greater the reliance</b>, auditor places on <b>operating effectiveness</b> of controls, greater is the extent of auditor’s TOC or <b>Higher</b> the auditor’s <b>assessment of ROMM</b>, <b>larger the sample size</b> needs to be</li> <li>• When <b>stratification</b> of population is appropriate then <b>sample size will decrease</b></li> </ul>	<p><b>Sample Selection Methods</b></p> <ul style="list-style-type: none"> <li>• <b>Random Sampling</b> - Random selection ensures that all items in population have a <b>known chance of selection</b>. It includes two methods which are –             <ul style="list-style-type: none"> <li>○ <b>Simple Random Sampling</b> - Under this method each unit of whole population has <b>an equal chance</b> of being selected. It is suitable for a <b>homogeneous population having a similar range</b></li> <li>○ <b>Stratified Sampling</b> - <b>Dividing heterogeneous</b> population into homogeneous sub population, where samples are drawn from each sub population. Each sub-population is called <b>stratum</b> and units under those sub-population are called <b>strata</b></li> </ul> </li> <li>• <b>Interval or Systematic Sampling</b> – In this, number of sampling units in <b>population is divided by sample</b></li> </ul>

<ul style="list-style-type: none"> <li>• If there is an <b>increase in tolerable rate of deviation/ tolerable misstatement</b>, then sample size will <b>decrease</b></li> <li>• <b>Higher the expected rate of deviation/ expected misstatements, larger</b> the sample size needs to be</li> <li>• An <b>increase in auditor's desired level of assurance</b> that tolerable rate of deviation/ tolerable misstatements is not exceeded by actual rate of deviation/ actual misstatements, will <b>increase the sample size</b></li> <li>• There will be <b>negligible effect</b> on sample size due to <b>increase in number of sampling units</b> in population</li> </ul>	<p><b>size to give a sampling interval</b>, for e.g. 50, and having determined a starting point within the first 50, each 50th sampling unit thereafter is selected. Auditor would need to determine that sampling interval does not correspond with a particular pattern in population. To minimise such risk, more than 1 starting points may be taken</p> <ul style="list-style-type: none"> <li>• <b>Monetary Unit Sampling</b> - It is a type of <b>value-weighted selection</b>. It identifies sampling unit as <b>individual monetary units</b> that make up population. Audit effort is directed to <b>larger value items</b> because they have a <b>greater chance of selection</b>, and can result in smaller sample sizes</li> <li>• <b>Haphazard sampling</b> - In this, auditor selects sample <b>without following a structured technique</b>. It is not appropriate when using statistical sampling</li> <li>• <b>Block Sampling</b> - It involves <b>selection of a block(s) of contiguous (adjacent) items</b> from population. It <b>cannot ordinarily be used</b> because a sequence in population can be expected to have similar characteristics to each other, but diff characteristics from items elsewhere in population</li> </ul>
<p><b>Performing Audit Procedures</b></p> <ul style="list-style-type: none"> <li>• Auditor shall perform audit procedures <b>on each item selected</b></li> <li>• If audit procedure is <b>not applicable</b> to selected item, auditor shall perform procedure <b>on a replacement item</b></li> <li>• If auditor is <b>unable to apply</b> audit procedures or alternative procedures to a selected item, auditor shall <b>treat</b> that item as <b>deviation from prescribed control</b>, in case of TOC <b>or misstatement</b> in case of TOD</li> </ul>	<p><b>Projecting Misstatements</b></p> <ul style="list-style-type: none"> <li>• Auditor is required to project misstatements to <b>obtain a broad view of scale of misstatement</b></li> <li>• When a misstatement has been established as <b>anomaly</b>, it may be <b>excluded when projecting</b> misstatements. However, if <b>uncorrected</b>, still need to be <b>considered in addition</b> to projection of non-anomalous misstatements</li> <li>• For <b>TOD</b>, auditor shall <b>project misstatements</b> found in sample to population whereas for <b>TOC, no explicit projection of deviations</b> is necessary since sample deviation rate is also projected deviation rate for population as a whole</li> </ul>
<p><b>Nature &amp; Cause of Deviations &amp; Misstatements –</b></p> <ul style="list-style-type: none"> <li>• Auditor shall <b>investigate nature &amp; cause</b> of deviations or misstatements &amp; evaluate their possible <b>effect</b></li> <li>• In extremely rare circumstances, when auditor considers misstatement or deviation to be an <b>anomaly</b>, auditor shall <b>obtain high degree of certainty</b> that such misstatement or deviation is <b>not representative of population</b></li> </ul>	<p><b>Evaluating Results of Audit Sampling - Auditor shall evaluate</b></p> <ul style="list-style-type: none"> <li>• <b>Results</b> of sample</li> <li>• Whether use of audit sampling has provided a <b>reasonable basis for conclusions about population</b></li> </ul> <p>If auditor concludes that <b>sampling has not provided reasonable basis</b> for conclusions about population that has been tested, auditor may -</p> <ul style="list-style-type: none"> <li>• <b>Request Mgt to investigate</b> misstatements that have been <b>identified &amp; potential</b> for further misstatements or</li> <li>• <b>Tailor NTE of FAP</b> to achieve required assurance</li> </ul>



<p><b>Related Party</b></p> <p>A party that is either -</p> <ul style="list-style-type: none"> <li>• A RP as defined in <b>AFRF</b> or</li> <li>• Where AFRF establishes minimal or no RP requirements –             <ul style="list-style-type: none"> <li>○ A person or <b>entity that has control or significant influence</b>, directly or indirectly through one or more intermediaries, over reporting entity</li> <li>○ Another <b>entity over which reporting entity has control or significant influence</b>, directly or indirectly through one or more intermediaries</li> <li>○ Another entity that is under <b>common control</b> with reporting entity through having –                 <ul style="list-style-type: none"> <li>▪ Common controlling <b>ownership</b></li> <li>▪ Owners who are <b>close family members</b></li> <li>▪ Common <b>Key Mgt</b></li> </ul> </li> </ul> </li> </ul> <p>However, entities that are under <b>common control by a state</b> (i.e. national, regional or local Govt) <b>are not considered related unless</b> they engage in <b>significant transactions</b> or <b>share resources</b> to a significant extent with one another</p>	<p><b>Meaning of control and significant influence</b></p> <ul style="list-style-type: none"> <li>• Control is <b>power to govern financial and operating</b> policies of an entity</li> <li>• Significant influence is <b>power to participate in financial and operating</b> policy decisions of entity, but is not control over those policies</li> </ul> <p><b>Whether FRF establishes A/c &amp; Disclosure requirements for RP relationships, transactions &amp; balances</b></p> <ul style="list-style-type: none"> <li>• If <b>Yes</b>, Auditor shall perform audit procedures to identify, assess &amp; <b>respond to ROMM</b> from <b>entity's failure to appropriately account</b> for or disclose RP relationships, transactions &amp; balances</li> <li>• If <b>No</b>, Auditor should <b>obtain understanding</b> of RP relationships and transactions to conclude whether FS give true &amp; fair view &amp; are not misleading</li> </ul>
<p><b>Engagement team discussion while understanding Entity's RP Relationships shall include susceptibility of FS to MM</b></p> <ul style="list-style-type: none"> <li>• <b>Nature &amp; extent</b> of entity's <b>relationships</b> &amp; transactions with RP</li> <li>• Records that may indicate <b>existence of RP relationships</b> or transactions</li> <li>• Circumstances that may indicate <b>existence of RP that Mgt has not disclosed to auditor</b></li> <li>• An emphasis on importance of <b>maintaining professional skepticism</b></li> <li>• <b>Importance</b> that Mgt &amp; TCWG attach to <b>appropriate A/cing for of RP</b> relationships &amp; transactions</li> </ul>	
<p><b>Identification of previously unidentified or undisclosed RP transactions</b></p> <ul style="list-style-type: none"> <li>• Auditor shall determine whether circumstances <b>confirm existence of such transactions</b></li> <li>• Communicate within <b>team</b></li> <li>• <b>Reconsider risks</b> with respect to other related parties</li> <li>• Request Mgt to <b>identify all transactions</b> with newly identified RP</li> <li>• Perform more <b>substantive procedures</b></li> <li>• If non-disclosure by Mgt <b>appears intentional, evaluate implications</b> for audit</li> </ul>	<p><b>Identified significant RP transactions outside entity's normal course of business</b></p> <ul style="list-style-type: none"> <li>• <b>Inspect</b> underlying <b>contracts</b> &amp; evaluate –             <ul style="list-style-type: none"> <li>○ <b>Business rationale</b> of transactions</li> <li>○ Whether <b>terms</b> of transactions are <b>consistent with Mgt's</b> explanations</li> <li>○ Whether such transactions have been <b>properly accounted</b> for</li> </ul> </li> <li>• Obtain audit evidence that transactions have been <b>appropriately authorised &amp; approved</b></li> </ul>
<p><b>Written Representation</b></p> <ul style="list-style-type: none"> <li>• <b>All RP &amp; transactions</b> have been <b>disclosed</b> to auditor</li> <li>• All such transactions have been <b>properly accounted for and disclosed in FS</b></li> </ul>	<p><b>Communication with TCWG</b></p> <p>Auditor shall communicate with TCWG <b>significant matters</b> arising during audit in connection with <b>entity's RP</b></p>
<p><b>Documentation - Names of RP &amp; Nature of RP transactions</b></p>	