SA 520.

Examples → NOV 22 (3 marks)

reliability of data → may 2 (3 marks)

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Analytical Procedure

Q Why do we need analysis?

⇒ Routine check → can't disclose all mistake | manipulation in TODs (sample)

↓

also certain procedure like comparison, trend & ratio analysis also required.

Meaning or definitation :→

(i) Analytical Procedure means evaluation of FI through analysis of Plausible (logical) relationship among both financial & non financial data.

[eg → Total wages (₹) → no. of workers → Non financial
→ wages per worker → financial]

(ii) Analytical Procedure also ecompass such investigation if

(a) Identified fluctuations, [eg → sales revenue CY ↑ 50% (year on year) ← Risk of fake sale
Generally → 10% ↑ [assumed → no. of store & customer same]]

(b) Relationship inconsistent with other info" &
[sales 50% ↑ COGS 20% ↓ ← Risk of overstated
Generally sales ↑ COGS ↑]

(c) differ from expected values by significant amount
[Hotel ← Expected revenue ⇒ 1.5 cr
Actual revenue ⇒ 2.5 cr) differ → 1 cr]

↓

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(iii) Analytical Procedure also includes the following :-

comparison of entity's FI
(i) Prior period
(ii) Budgets/forcasts/expectations
(iii) Similar industry info^n.

[eg → comparison of entity's ratio of sales to a/c receivable
• with industry average or
• other entities in same industry]

Consideration of relationship
Among elements of FS expected to confirm to Predictable Pattern
[eg - Gross margin %]
Betw^n financial & relevent non financial info^n,
[eg - Payroll cost to no. of employees]

Various other Procedures.

(iv) Segregation of Analytical Procedures into :-

MCQs

(a) Comparison of client data with industry data
(b) " similar prior period data (CY & PY)
(c) " client determined expected results
(d) " auditor determined expected results
(e) " Expected results, using non-financial data [eg (Goods sold qty ↑ 40% . ↑ Sales 40% ↑)]

Scope of SA

Objective of Auditor :- (i) to obtain relevent & reliable AE when using SAP & [Testing or execution Phase]

(ii) to design & perform analytical Procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the FS are consistent with the auditors understanding of the entity. [Completion Phase].

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RTP May 25

PURPOSE :-

may 22

I. Q Auditor compares P&L item of CY with PY why?

⇒ Analytical Procedures use comparison & relationship to assess whether a/c bals or other data appear reasonable.

eg :- • If P&L Bals of CY compared with PY, it will be to find (i) reasons of ↑/↓ in Profits.

(ii) • If expense ratios of P&L can be compared with PY, to know ↑/↓ in expense item in relation to sales and trading Profit to sale

① ↑↓ reason

② If the difference are material (i) ascertain reason &
(ii) assess if a/c manipulated to inflate / suppress the profits

③ It may be possible to identify unusual or unexpected
(i) txn, events, amounts, ratios, trends have audit implications
(ii) relationships which may assist auditor in → detecting those areas where RMM can be high specially due to fraud.

II. Q An abnormal fall in cost of manufacture or Administration cost, apart from economy in expenses

- There could be no provision or less provision for expense in the CY. when its suspected, compare the entities in outstanding book with PY.
- He must also check vouchers for 1 month immediately before close of following year. To verify that none of the expense in a/cs under audit have been charged to following years.

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Dec 21

III. Q Analytical Procedures helps in Independent verification of P&L item ?

Imports on custom duty	GST paid on Sales	Comm or Bonus paid to manager
⇓	⇓	⇓
cost of imports subject to advalorem duty [Based on value] at uniform rat can be verified from duty paid.	Qty of sugar sold can be verified from GST paid	Amt of any income/expense which has direct relation with Profit or sales. [eg - mgmt comm on Basis of NP etc].

Corroborate → additional evidence to support primary evidence.

Timing of Analytical Procedure

Planning Phase
RAP → 315 SA
(identify RMM)

Analytical Procedure in planning the audit :-

(a) Auditor can use analytical procedure in planning phase to understand the entity's business to identify areas of potential risk which auditor may not be previously aware of.

(b) Analytical Procedure will assist the auditor in determining NTE of other AP.

(c) Auditor may use both financial & non financial data for the purpose of the analysis
(eg - no. of employees, total qty produces, total sq ft of area cite business etc).

Execution Phase
SAP (testing) → SA520

* Steps to apply substantive analytical Procedure (SAP) during Testing or Execution Phase :-
[Analytical Procedure used as substantive test]

(i) Determine suitability of analytical Procedure :- **XX**
- Determine the suitability of a particular SAP for a given assertion [eg - inventory, Payroll exp, electricity exp]
- Auditor should take into account assessed RMM & relevent TOD before choosing the SAP.

(ii) Evaluate Reliability of data :-
- Evaluate the reliability of data which auditors expectation of recorded amount is developed.

* Auditor should consider the following factors to determine reliability of data for purpose of designing SAP :- (may 23)

(a) Source of info^n :-
Independent sources are more reliable

(b) Comparability of info^n :-
[eg - we should not use general or board industry data rather, such data should be appropriately supplemented].

(c) Nature & relevance of info^n :-
[eg - assumptions use for making budgets should be realistic.

(d) Controls over the preparation of info^n :-
- to ensure its completness & accuracy.
- if controls are effective the info^n will be reliable
[eg - review & maintenance of budget].

Completion Phase.
(At the end of audit for conclusion) — SA520

Auditor can use analytical Procedure during completion phase to corroborate conclusion formed audit of individual components or elements of FS.

(iii) Develop an expectation :-
- Develop an expectation of recorded a/c & evaluate whether expectation of auditor is sufficiently precised to identify MMs.
[MS may be material either individually or when aggregated with others.]

* factors or matters which are relevent while ensuring the auditors expectations is sufficiently precised :- (RTP may 22)

(a) The accuracy with which the expected results of SAP can be predicted.
[eg → The auditor may expect greater consistency in comparing GP margins from one period to another period in comparing discretionary expenses, such as research or advertisment]

(b) The degree to which info^n can be disagreed (eg -)

(c) The availability of the info^n, both F & NF. (eg -)

Refer module Pg - 4.123.

(iv) Determine acceptable difference :-
- Determine the amount of materiality to compare & conclude whether the difference betw^n recorded amount & auditor expected amount requires any further investigation or is acceptable as it is.

* Amount of difference acceptable w/o investigation

(a) Materiality.	materiality ↑ → AODA ↑
(b) Desired level of assurance	wants ↑ → AOD ↓
(c) RMM	RMM ↑ → AODA ↓

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XX Suitability of Particular analytical Procedure for given assertion :-

(i) SAP are generally more applicable to large volumes of tx^n that tend to be predictable overtime.

(ii) The application of planned analytical procedure is based on the expectation that relationships among data exist & continue in the absence of known conditions to the contrary.

(iii) However, the suitability of a particular analytical procedure will depend upon the auditor's assessment of how effective it will be in detecting a MS that, (individually or when aggregated with other MS), may cause the FS to be MMS.

(iv) In some cases, even an unsophisticated predictive model may be effective as an analytical Procedure.

(v) $Diff^n$ types of analytical Procedures provide $diff^n$ levels of assurance.

(vi) The suitability of particular SAP is influenced by the nature of the assertion & the auditor's assessment of the RMM.

(vii) Particular SAP may also be considered suitable when TOCs are performed on the same assertion.

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MTP NOV22

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Investigating results of Analytical Procedures :->

As per SA 520 after identifying any fluctations or inconsistency in the financial infoⁿ or when the difference between auditor expected amount and actual recorded amount is significant then auditor should follow the following steps:->

(a) Auditor should enquire with the mgmt & obtain SAAE to understand the reasons for such differences including the validity of mgmt response.

(b) Auditor can also plan to perform other AP as may be necessary in the circumstances, Generally these additional procedure will be required when mgmt does not provide any explanations or provide inadequate evidences as response.

Analytical Procedures that assist when Forming an Overall Conclusion:-

- Conclusions drawn from results of analytical procedures are intended to corroborate conclusions formed during audit of individual components of FS.
- This assits auditor to draw reasonable conclusions to base auditors opinion.
- Result of such analytical procedures may identify a previously unrecognised RMM.

In such circumstances, SA 315 requires auditor to revise auditor's assessment of RMM & modify FAP.

NOV20

Factors to be considered while Performing SAP :-

1. Availability of Data :- Only if reliable and relevent data, data is available then Substantive Analytical Procedure can become effective.

2. Disaggregation of Data :- The degree of disaggregation in available data can directly affect its usefulness in detecting MS using analytical Procedure.

3. Type of assertion (or) Account Type :- Income statement are more predictable because they reflect accumulated amount of all txn that have taken place during the year while in case of balancesheet line items net effect of Txn is identified.
[note: areas where significant mgmt judgement is involved are also not suitable for SAP.

MCQ

4. Source (nature of Txn) :- routine nature of txn are more predictable than non-routine or those txn which involves significant mgmt judgement.

5. Predicability or existence of logical relationship :- such as sales commission related to sales.

6. Inherent risk or "what can go wrong" :- If auditor determines Inherent risk and respective RMM to be high for a specific area then ~~desg~~ relying solely on AE obtained from SAP will be inappropriate therefore auditor should plan to perform more of TODs.

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Techniques available for performing SAP :-

(a) Trend Analysis :-

(i) In this technique auditor can compare current year data with prior period amount or with a trend with which is visible in two or more prior period balances.

(ii) eg :- comparing payroll expense of current year with prior period data.

MCQs

(b) Reasonableness Test :-

(i) In this technique auditor will use certain non-financial data related to the current period to develop and expectations of financial amount.

(ii) for eg :- calculating or estimating rental revenue based on occupancy of premises.

- wastage or scrap as % of total prodn or raw material consumption.

(c) Ratio Analysis :-

(i) It is a technique use to analysis asset, and liability account as well as revenue & expense accounts.

(ii) for eg :- inventory T/o ratio, freight expenses as a % of revenue etc.

(iii) Auditor can compare ratios of prior period with the current period or with industry ~~data~~ ratio.

(d) Structural Modelling :-

Auditor can also use specific statical model from prior period financial data & non-financial data to predict the current year account balances. (liner regression), (Depreciation Globe check to estimate the current period depreciation amount.)