

Chapter - 2

"Audit Strategy, Planning & Execution"

(1)	<u>Audit Planning:</u>
(i)	<u>Meaning:</u>
	(a) Developing an overall plan for the expected scope & conduct of audit and
	(b) Developing an audit programme showing NTE of Audit procedures
(ii)	<u>Importance of planning:</u>
	(a) To devote attention to important areas.
	(b) Identify & resolve potential problems.
	(c) Organized and managed audit.
	(d) Selection of suitable ET members with appropriate levels of skills.
	(e) Coordination of work done by auditors of components and experts.
	(f) Direction & supervision of engagement team members and review of their work.
(iii)	<u>Factors affecting Nature & Extent of Planning:</u>
	(a) Size and Complexity of Auditee (Client).
	(b) Past Experience
	(c) Changes in Circumstances
(iv)	<u>Factors to be considered in development of overall plan:</u>
	(a) Terms of engagement and statutory responsibilities.
	(b) Nature & timing of reports and other communications.
	(c) Legal or statutory requirements.
	(d) Accounting policies & changes therein.
	(e) Effects of new accounting/auditing pronouncements.
	(f) Identification of significant audit areas.
	(g) Setting of materiality levels for the audit purposes.
	(h) Degree of reliance to be placed on accounting system and internal control.
	(i) Nature and extent of audit evidence to be obtained.

(2)	<u>Audit Strategy:</u>
(i)	<u>Meaning:</u>
	Designing Audit Approaches to achieve necessary audit assurance at the lowest cost.
(ii)	<u>Steps involved in Audit Strategy:</u>
Step - 1:	<u>Obtaining knowledge of business:</u>
	It provides a frame of reference within which auditor exercises his professional judgment to assess risk, to plan audit, to evaluate audit evidence & provide quality services to the client.
Step - 2:	<u>Performing Analytical Procedures at Initial Stages:</u>
	To assess the potential for material misstatement in the F.S. as a whole.
	<p>Note: The use of analytical procedures during the planning stage requires the extensive use of accounting and business knowledge and experience to assess the potential for material misstatement in the financial statements as a whole, because the key aspect of the task is to identify the relevant risk indicators and to interpret them properly.</p>
Step - 3:	<u>Evaluating Inherent Risk:</u> On the basis of
(a)	prior audit experience,
(b)	controls exercised by management,
(c)	significant changes since last assessment.
Step - 4:	<u>Evaluating IC System:</u>
	By documenting extent of computerization, preparing / updating flowcharts to record the transactions.
	<p>Note: The auditor needs an understanding of the accounting systems, regardless of whether the audit strategy will involve an extended assessment of internal accounting controls.</p>

	Step - 5: <u>Formulating Audit Strategy:</u>
	Requires consideration of:
	(a) Engagement objective
	(b) Knowledge of client's business
	(c) Preliminary judgments as to materiality
	(d) Identified inherent risks
	(e) Extent of compliance testing
	(f) NTE of Substantive testing
	(g) Points relating to planning and controlling the audit.
	(iii) <u>Benefits of Audit Strategy:</u>
	(a) Employment of Qualitative Resources.
	(b) Allocation of appropriate quantity of resources.
	(c) Determining the timing of deployment of resources.
	(d) Better management of resources in terms of direction, supervision, timing of team meetings etc.
	(iv) <u>Relationship between Audit Strategy & Audit Planning</u>
	- Audit strategy and audit plan are inter-related to each other because change in one would result into change in the other.
	- The audit strategy is prepared before the audit plan. The audit plan contains more details than the overall audit strategy.
	- The audit strategy provides the guidelines for developing the audit plan.
	- Audit strategy establishes the scope, timing and direction of the audit and thereby works as basis for developing a detailed audit plan.
	- Detailed audit plan would include the nature, timing and extent of the audit procedures so as to obtain sufficient appropriate audit evidence.

(3) <u>Audit Programming:</u>	
(i) <u>Meaning:</u>	
(a)	Detailed plan of work prepared by auditor for carrying out an audit.
(b)	Audit programme comprises of techniques and procedures.
(c)	It may also contain objectives for each audit step.
(ii) <u>Matters to be considered in formulating Audit programme:</u>	
(a)	Nature of business in which the organisation is engaged.
(b)	Overall Plan prepared for the audit.
(c)	System of internal control and accounting procedures.
(d)	Size and structure of organization.
(e)	Information regarding the organization of business.
(f)	Accounting policies followed.
(iii) <u>Development of Audit programme:</u>	
(i) <u>First Time Audit:</u>	
(a)	Draw a broad outline
(b)	Filled up the details on a consideration of deficiencies in internal control.
(c)	Determine the special procedures needs to be applied.
(ii) <u>Subsequent Engagement:</u>	
	Review earlier programme and modified on account of:
(a)	Experience gained during the previous audit.
(b)	Important changes in internal control system, accounting procedures etc.
(c)	Evaluation of internal control for current year.

	(iv) <u>Circumstances requiring changes in Audit Programme:</u>
	(a) Substantial increase in Volume of turnover.
	(b) Significant changes in accounting procedures.
	(c) Observation w.r.t. ineffective internal control.
	(d) Substantial increase in book debts or inventory.
	(e) Suspicion as to misappropriation of assets.
	(4) <u>Stages of Audit Execution:</u>
	Stage - I: <u>Execution Planning:</u>
	During execution planning, auditor should consider manpower requirement, qualification of members of ET, time factor etc.
	Stage - II: <u>Risk and Control Evaluation:</u>
	Auditor need to conduct a detailed assessment of risk and control as per requirements of SA 315.
	Steps involved in assessment of risk are:
	(a) List the risk that need to be reviewed for each segment of audit.
	(b) Capture for each risk the controls that exist or those that are needed
	(c) Determine the steps required to test the effectiveness of each controls.
	Note: While making Risk & Control assessment auditor need to consider the <u>Materiality levels.</u>
	Stage - III: <u>Testing:</u>
	(a) As required by SA 330, auditor should test operating effectiveness of internal control to determine whether controls are operating as designed.
	(b) Auditor should perform appropriate substantive procedures (ToD and SAP) so as to collect SAAE w.r.t. completeness, accuracy and validity of accounting data.

Stage - IV: Reporting:

- (a) The auditor should review and assess the conclusions drawn from the audit evidence obtained as the basis for the expression of an opinion on the F.S.
- (b) Opinion so farmed should be expressed in form of audit report as required by SA 700.

DO Practice - Questions on Audit Planning, Strategy and Programming

