

AUDIT PLANNING

STRUCTURE:

- 3.0 Objectives
- 3.1 Meaning:
- 3.2 Objectives Of Planning
- 3.3 Factors To Be Considered
- 3.4 Sources Of Obtaining Information
- 3.5 Development Of An Overall Plan
- 3.6 Meaning Of Audit Programme
- 3.7 Factors Advantages And Disadvantages Of Audit Programme
- 3.8 Audit Working papers

3.0 OBJECTIVES

After studying the unit the students will be able to

- Define Audit Planning
- Understand the Objectives of Audit Planning
- Understand the Meaning of Audit Programme
- Explain the factors, advantages and disadvantages of Audit Programme
- Know the meaning of Audit Papers.

3.1 MEANING

As per Auditing and Assurance Standard 1, “Basic Principles Governing an Audit”, Audit Planning is one of the basic principles. Accordingly, it states

“The auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. Plans should be based on knowledge of the client’s business. Plans should be made to cover, among other things:

(a) Acquiring knowledge of the client’s accounting systems, policies and internal control procedures;

(b) Establishing the expected degree of reliance to be placed on internal control;

(c) Determining and programming the nature, timing, and extent of the audit procedures to be performed; and

(d) Coordinating the work to be performed.

Plans should be further developed and revised as necessary during the course of the audit.”

AAS-8 further expounds this principle. According to it, planning should be continuous throughout the engagement and involves

- Developing an overall plan for the expected scope and conduct of the audit; and
- Developing an audit programme showing the nature, timing and extent of audit procedures.

Changes in conditions or unexpected results of audit procedures may cause revisions of the overall plan of and the audit programme. The reasons for significant changes may be documented.

3.2 OBJECTIVES OF PLANNING

Adequate audit planning helps to:

- Ensure that appropriate attention is devoted to important areas of the audit.
- Ensure that potential problems are promptly identified;
- Ensure that the work is completed expeditiously;
- Utilize the assistants properly; and
- Co-ordinate the work done by other auditors and experts.

In planning his audit, the auditor will consider factors such as complexity of the audit, the environment in which the entity operates his previous experience with the client and knowledge of the client's business.

The auditor may wish to discuss elements of his overall plan and certain audit procedures with the client to improve the efficiency of the audit and to coordinate audit procedures with work of the client's personnel. The overall audit plan and the audit programme, however, remain the auditor's responsibility.

3.3 FACTORS TO BE CONSIDERED

_Planning his audit, the Auditor will consider the following factors -

Complexity of the Audit: The scope of work and reporting responsibilities is analysed in order to determine the complexity of audit.

Environment in which the entity operates: This enables the Auditor to understand various operational aspects of audit, e.g. extent of computerization, nature of internal controls, general attitude of personnel, etc.

Previous experience with the client: By analysing the previous year's audit working papers and other relevant files, the Auditor should pay

particular attention to matters that required special consideration and decide whether they might affect the work to be done in the current year.

Knowledge of the client's business: This is required to establish the overall audit plan. The Auditor will be able to - (a) identify areas of special audit consideration, (b) evaluate the reasonableness both of accounting estimates and management representations, and (c), make judgments regarding the appropriateness of accounting policies and disclosures.

Discussion with Client: The Auditor can discuss his overall plan and certain audit procedures with the client to improve the efficiency of the audit and to coordinate audit procedures with work of the client's personnel. The overall audit plan and the audit Programme, however, remain the Auditor's responsibility.

3.4 SOURCES OF OBTAINING INFORMATION

Sources of information listed under AAS - 8: The Auditor should obtain a level of knowledge of the client's business that will enable him to identify the events, transactions and practices that, in his judgment, may have significant effect on the financial information. The Auditor can gain knowledge of client's business from –

The client's Annual Reports to Shareholders.

Minutes of Meetings of Shareholders, Board of Directors and important Committees.

Internal Financial Management Reports for current and previous periods, including Budgets, if any.

Previous year's Audit Working Papers, and other relevant files.

Key Personnel responsible for non-audit services to the client who may be able to provide information on

matters that may affect the audit.

Discussions with Client.

Client's Policy and Procedures Manual.

Relevant publications of the ICAI and other professional bodies, Industry Publications, Trade Journals,

Magazines, Newspapers or Textbooks.

Consideration of the state of the economy and its effect on the client's business.

Visits to the client's premises and plant facilities.

Discussion with client:

ording to AAS - 8, during the course of planning the audit, discussions with the client might include the wing subjects -

Changes in Management, Organisational Structure, and activities of the client.

Current Government Legislation, Rules, Regulations and Directives affecting the client.

Current Business Developments affecting the client.

Current or impending Financial Difficulties or Accounting Problems.

Existence of Interested Parties and transactions with them.

3.5 DEVELOPMENT OF AN OVERALL PLAN

The auditor should consider the following matters in developing his overall plan for the expected scope and conduct of the audit:

- The terms of his engagement and any statutory responsibilities.
- The nature and timing of reports or other communication.
- The applicable legal or statutory requirements.
- The accounting policies adopted by the client and changes in those policies.
- The effect of new accounting or auditing pronouncements on the audit.
- The identification of significant audit areas.
- The setting of materiality levels for audit purposes.
- Conditions requiring special attention, such as the possibility of material error or fraud or the involvement of parties in whom directors or persons who are substantial owners of the entity are the act of examining vouchers is referred to as vouching. It is the practice followed in an audit, with the objective of establishing the authenticity of the transactions recorded in the primary books of account. It essentially consists of verifying a transaction recorded in the books of account with the relevant documentary evidence and the authority on the basis of which the entry has been made; also confirming that the amount mentioned in the voucher has been posted to an appropriate account which would disclose the nature of the transaction on its inclusion in the final statements of account. On these considerations, the essential points to be borne in mind while examining a voucher are:

- (i) That the date of the voucher falls within the accounting period;
- (ii) That the voucher is made out in the client's name;
- (iii) That the voucher is duly authorized;
- (iv) that the voucher comprised all the relevant documents which could be expected to have been received or brought into existence on the transactions having been entered into, i.e., the voucher is complete in all respects; and
- (v) That the account in which the amount of the voucher is adjusted is the one that would clearly disclose the character of the receipts or payments posted thereto on its inclusion in the final accounts.

After the examination is over, each voucher should be either impressed with a rubber stamp or initialed so that it may not be presented again in support of another entry.

3.6 MEANING OF AUDIT PROGRAMME

MEANING:

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 nothing but a list of examination and verification steps to be applied set out in such a way that the inter-relationship of one step to another is clearly shown and designed, keeping in view the assertions discernible in the statement of account produced for audit or on the basis of an appraisal of the accounting records of the client. In other words, an audit programme is a detailed of the accounting records of applying the audit procedures in the given circumstances with instructions for the appropriate techniques to be adopted for accomplishing the audit objectives. Businesses vary in nature, size and composition; work which is suitable to one business may not be suitable to be rendered by the auditor are the other factors that vary from assignment to assignment. Because 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 details 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.

An audit programme consists of a series of verification procedures to be applied to the financial statements and accounts of a given company for the purpose of obtaining sufficient evidence to enable the auditor to

express an informed opinion on such statements. For the purpose of programme construction, the following points should be kept in view:

1. stay within the scope and limitation of the assignment.
2. determining the evidence reasonable available and identify the best evidence for deriving the necessary satisfaction.
3. Apply only these steps and procedures which are useful in accomplishing the verification purpose In the specific situation.
4. consider all possibilities of error.
5. co-ordinate the procedures to be applied to related items.

Amplification is not necessary of the above points except the one under evidence: that 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 experts knowledge and evidence. 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 reasonable available in respect of each transaction

3.7 FACTORS ADVANTAGES AND DISADVANTAGES OF AUDIT PROGRAMME

3.7.1 FACTORS

While construction an audit programme, the Auditor should keep the following points in his mind-

1. to operate within the scope and limitations of the assignment.
2. to determine the evidence reasonably available and identify the best evidence for deriving the necessary satisfaction.
3. to apply only those steps and procedures, which are useful in accomplishing the verification purpose in the specific situation.
4. to consider all possibilities of error.
5. to co-ordinate the procedures to be applied to related items.

3.7.2 ADVANTAGES OF AUDIT PROGRAMME

- 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 compatibility 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, the danger is significantly less and the audit can proceed systematically.
- e. The assistance, by putting their signature on programme, accepts 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.

3.7.3 DISADVANTAGES OF AUDIT PROGRAMME

- 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 or 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 instructions 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 observed matters objectively and bring significant matters to the notice of supervisor/principal.

3.8 AUDIT WORKING PAPERS

3.8.1 MEANING:

The audit working papers constitute the link between the auditor's report and the client's records. Documentation is one of the basic principles listed in AAS 1. according to AAS 3 (reproduced in Appendix I), documentation refers to working papers prepared or obtained by the auditor and retained by him in connections with performance of his audit. The objects of an auditor's working papers are to record and demonstrate the audit work from one year to another. Therefore, working papers should provide for:

- a) Means of controlling current audit work;
- b) Evidence of audit work performed;
- c) Schedules supporting or additional item in the accounts; and
- d) Information about the business being audited, including the recent history.

Working papers are varied in nature but the foundation of all working paper can be traced to:

- 1. the basic constitutional document like memorandum and Articles of association, partnership Deed, trust deed, etc.;
- 2. the contents of the minute books;
- 3. the contents of the balance sheet and the profit and loss account; and
- 4. the letter of engagement.

3.8.2 IMPORTANCE OF AUDIT WORKING PAPERS:

- I. IT provides guidance to the audit staff regard to the manner of checking the schedules.
- II. The auditor is able to fix responsibility on the staff member who signs each schedule checked by him.

- III. It acts as an evidence in the court in the court of law when a charge of negligence is brought against the auditor.
- IV. It acts as the process of planning for the auditor so that he can estimate the time that may be required for checking the schedules.

The auditor should adopt reasonable procedures for custody and confidentiality of his working papers and should retained them for a period of time sufficient to meet the needs of his practice and satisfy any pertinent legal or professional requirements of record retention.

3.8.3 FACTOR DETERMINING FORM AND CONTENTS OF AUDIT WORKING PAPERS:

Working papers should record the audit plan, nature, timing and extent of auditing procedures performed, and the conclusions drawn from the evidence obtained. The form and content of working papers are affected by matters such as:

- Nature of the engagement.
- Form of the auditor's report.
- Nature and complexity of the client's business.
- Nature and condition of the client's records and degree of reliance on internal controls.
- Need in particular circumstances for direction, supervision and review of work performed by assistants.

Working papers should be designed and properly organized to meet the circumstances of each audit and the auditor's needs in respect thereof. The standardization of working papers (for example, checklists, specimen letters, standard organisation of working papers) improves the efficiency with which they are prepared and reviewed. It also facilitates the delegation of work while providing a means to control its quality. Working papers should be sufficiently complete and detailed for an auditor to obtain an overall understanding of the audit. The extent of the documentation is a matter of professional judgement since it is neither necessary nor practical that every observation, consideration, consideration or conclusion is documented by the auditor in his working papers.

3.8.4 A Permanent Audit File

A permanent audit file normally includes

- ◆ Information concerning the legal and organizational structure of the entity. In case of a company, this includes the memorandum and Article of association. In the case of a statutory corporation, this includes the act and regulations under which the corporation functions.
- ◆ Extracts or copies of important legal documents, agreements and minute relevant to the audit.
- ◆ A record of the study and the evaluation of the internal controls related to the accounting system. This might be in the form of narrative descriptions, questionnaires or flow charts, or some combination thereof.
- ◆ Copies of audited financial statements for previous years.
- ◆ Analysis of significant ratios and trends.
- ◆ Copies of management letters issued by the auditor, if any.
- ◆ Record of communication with the retiring auditor, if any, before acceptance of the appointment as auditor.
- ◆ Notes regarding significant accounting policies.
- ◆ Significant audit observations of earlier years.

3.8.5 The Current File

The current file normally includes

- ◆ Correspondence relating to acceptance of annual reappointment.
- ◆ Extracts of important matters in the minutes of board meetings and general meetings as relevant to audit.
- ◆ Evidence of the planning of the audit and audit programme.
- ◆ Analysis of transactions and balances.
- ◆ A record of the nature, timing and extent of auditing procedures performed, and the results of such procedures.
- ◆ Evidence that the work performed by assistants was supervised and reviewed.
- ◆ Copies of communication with other auditors, experts and other third parties.
- ◆ Letters of representation or confirmation received from the client.
- ◆ Conclusions reached by the auditor concerning significant aspects of the audit, including the manner in which exceptions and unusual matters, if any, disclosed by the auditor's procedures were resolved or treated.
- ◆ Copies of the financial information being reported on the related audit reports.

3.8.6 MAIN FUNCTIONS/ IMPORTANCE

- i. It provides guidance to the audit staff with regards to the manner of checking the schedules.
- ii. The auditor is able to fix responsibility on the staff member who sign each schedule checked by him.
- iii. It acts as an evidence in the court of law when a charge of negligence is brought against the auditor.
- iv. It acts as the process of planning for the auditor so that he can estimate the time that may be required for checking the schedules.

The auditor should adopt reasonable procedures for custody and confidentiality of his working papers and should retain them for a period of time sufficient to meet the needs of his practice and satisfy any pertinent legal or professional requirement of record retention.

Clarification On The Auditor's Rights Where Clients And Other Auditors Seek Access To Their Audit Working Papers.

1. Auditing and Assurance standard (AAS) 1, "Basic principles governing an audit", states in para6: "The auditor should respect the confidentiality of information acquired in the course of his work and should not disclosed any such information to a third party without specific authority or unless there is a legal or professional duty to disclosed". Auditing and Assurance standard (AAS) 3, "Documentation" (paragraph 13), states: 'working papers are the property of the auditor. The auditor may at his discretion, make portions of or extracts from his working papers available to his client. "AAS 3 further requires (paragraph 14)",inter alia, that the "auditor should adopt reasonable procedures for custody and confidentiality of his working papers."

2. part I of the second schedule to the chartered Accountants Act, 1949, provides that "A Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he disclosed information acquired in the course of his professional engagement to any person other than his client, without the consent of his client or otherwise than as required by any law for the time being in force."

3. Request are sometime received by the members of the institute, who have/had been performing the duties as the auditor of an enterprises, to provide access to their audit working papers. The request may be made by the clients or other auditors of the enterprise or its related enterprise such as a parent enterprise.

4. It is hereby clarified that except to the extent stated in para 5 below, an auditor is not required to provide the client or the other auditors of the same enterprise or its related enterprise such as a parent or a subsidiary,

access to his audit working papers. The main auditors of an enterprise do not have right of access to the audit working papers of the branch auditors. In the case of a company, the statutory auditor has to consider the report of the branch auditor and has a right to seek clarifications and/or to visit the branch if he deems it necessary to do so for the performance of the duties as auditor. An auditor can rely on the work of another auditor, without having any right of access to the audit working papers of the other auditor. For this purpose, the term 'auditor' includes 'internal auditor'.

5. As stated in para 4, the client does not have a right to access the working papers of the auditor. However, the auditor may, at his discretion, in case considered appropriate by him, make portions of or extracts from his working papers available to the client.

3.8.7 FEATURES

As audit working papers are quite useful they should be prepared properly. They should have the following essentials:

- a) **Standard form** - they should be prepared in a standard form. The subject matter should be arranged under various heading and sub-headings.
- b) **Proper layout** – there should be proper design and layout of the working papers. This will bring uniformity into the maintenance of working papers.
- c) **Space for margins** – there should be enough space for margin after each note for noting down the auditor's remarks and decisions.
- d) **proper organisation and arrangement** – the working papers should be properly organized and arranged. In other words the working papers should be so organized and arranged that the auditor will be able to locate any particular matter easily.
- e) **Completeness** – the audit working papers should be complete in all respects. They should contain detailed information on all essential facts or points.
- f) **Clarity and Accuracy** – the working papers should be quite clear and self explanatory. The information contained in the working papers should be accurate.
- g) **Good quality paper** – paper of good quality should be used for working papers as they are subject to frequent handling further the paper used should be of uniform and convenient size so that they can be easily filed.

3.8.8 OWNERSHIP, AND CUSTODY OF WORKING PAPERS

Working papers are the property of the auditor. The auditor may, at his discretion may, at his discretion, make portions of or extracts from his working papers available to his client. Audit working papers are the

property of the auditor and he is entitled to retain them. (chantery martin & co. v. martin).

