

CA FINAL
NEW SCHEME - GROUP - I
ADVANCED AUDITING,
ASSURANCE AND
PROFESSIONAL ETHICS

MODULE - I

Chapters 1 to 11

3rd Edition

Author

CA Aarti N. Lahoti

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Price : Rs. 1495

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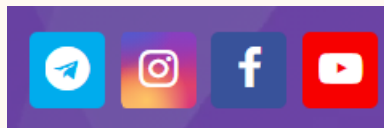
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CA Aarti N. Lahoti

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Aarti Lahoti



Dear Students,

IT'S ALL ABOUT AUDIT!

It gives me immense pleasure to present before you the 3rd Edition of Advanced Auditing, Assurance & Professional Ethics – Module I & II – for CA Final.

I have made an humble attempt to include all theory, Q & A & Amendments released by ICAI through its different mediums viz. Latest Study Material, Suggested Answers, Mock Test Papers & Revision Test Papers in this book.

Any constructive criticism is always welcome. @ aartilahoti9@gmail.com

The greatest strength of this book is its wholistic approach towards the subject – a one stop solution for the entire subject of CA Final Auditing. It covers each & every topic of the syllabus in a tabular & pointwise format & also the myriad varieties of questions in relation to the same.

*Having **CONCEPTUAL CLARITY** about the topics is half the battle won!!! To complete it you need to do a lot of **WRITING PRACTICE**. As a general problem faced by students is that though they understand the concepts but they are not able to put it in words & this happens merely due to lack of writing practice. So never forget that!*

*And one final piece of advice would be to do **CUMULATIVE REVISIONS** of the subject so that you are able to retain the subject better.*

Wishing you all the very best for your exams and for a brightful future!

Happy Auditing!

Regards,

CA Aarti N. Lahoti

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CA Aarti Lahoti Classes



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Chapter 0

INTRODUCTION & QUICK RECAP

1

LIST OF QUALITY CONTROL & ENGAGEMENT STANDARDS

No. of SQC/SA/SRE /SAE/SRS	Title of the Standard	Key words	Effective Date
1 – 99	STANDARDS ON QUALITY CONTROL (SQC)		
SQC 1	Quality Control for Firms that Perform Audits & Reviews of Historical Financial Information, & Other Assurance & Related Services Engagements.	Quality Control for Firms	01.04.2009
100 – 899	AUDITS & REVIEWS OF HISTORICAL FINANCIAL INFORMATION (SA)		
100 – 199	INTRODUCTORY MATTERS		
200 – 299	GENERAL PRINCIPLES & RESPONSIBILITY		
SA 200	Overall Objectives of the Independent Auditor & the Conduct of an Audit in Accordance with Standards on Auditing	Overall Objectives	01.04.2010
SA 210	Agreeing the Terms of Audit Engagements	Engagement Letter	01.04.2010
SA 220	Quality Control for an Audit of Financial Statements	Quality Control for an Audit	01.04.2010
SA 230	Audit Documentation	Documentation	01.04.2009
SA 240	The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements	Fraud	01.04.2009
SA 250	Consideration of Laws & Regulation in an Audit of Financial Statements	Laws & Regulations	01.04.2009
SA 260	Communications with Those Charged With Governance	TCWG	01.04.2017
SA 265	Communicating Deficiencies in Internal Control to Those Charged with Governance & Management	DIC – TCWG & Mgmt.	01.04.2010
SA 299	Joint Audit of Financial Statements	Joint Auditors	01.04.2018
300 – 499	RISK ASSESSMENT & RESPONSE TO ASSESSED RISKS		
SA 300	Planning an Audit of Financial Statements	Planning	01.04.2008
SA 315	Identifying & assessing the Risks of Material Misstatements through understanding the Entity & Its Environment	Risk Assessment	01.04.2008
SA 320	Materiality in Planning & Performing an Audit	Materiality	01.04.2010
SA 330	Auditor's Responses to Assessed Risks	Responses	01.04.2008
SA 402	Audit Considerations Relating to an Entity Using a Service Organisation	Service Organisation	01.04.2010
SA 450	Evaluation of Misstatements Identified During the Audit	Misstatements	01.04.2010
500 – 599	AUDIT EVIDENCE		
SA 500	Audit Evidence	Audit Evidence	01.04.2009
SA 501	Audit Evidence – Specific Considerations for Selected Items	Selected Items	01.04.2010
SA 505	External Confirmations	Confirmations	01.04.2010
SA 510	Initial Audit Engagements - Opening Balances	Opening Balances	01.04.2010
SA 520	Analytical Procedures	Analytical	01.04.2010
SA 530	Audit Sampling	Sampling	01.04.2009

SA 540	Auditing of Accounting Estimates, including Fair Value Accounting Estimates & Related Disclosures	Estimates	01.04.2009
SA 550	Related Parties	Related Parties	01.04.2010
SA 560	Subsequent Events	Subsequent Events	01.04.2009
SA 570	Going Concern	Going Concern	01.04.2017
SA 580	Written Representations	WR	01.04.2009
600 – 699	USING WORK OF OTHERS		
SA 600	Using the Work of Another Auditor	Branch Auditor	01.04.2002
SA 610	Using the work of Internal Auditors	Internal Auditors	01.04.2016
SA 620	Using the Work of an Auditor's Expert	Auditor's Expert	01.04.2010
700 – 799	AUDIT CONCLUSIONS & REPORTING		
SA 700	Forming an Opinion & Reporting on Financial Statements	Audit Report	01.04.2018
SA 701	Communicating Key Audit Matters in the Independent Auditor's Report	Key Audit Matters	01.04.2018
SA 705	Modifications to the Opinion in the Independent Auditor's Report	Modifications	01.04.2018
SA 706	Emphasis of Matter Paragraphs & Other Matter Paragraphs in the Independent Auditor's Report	EOM/OM	01.04.2018
SA 710	Comparative Information – Corresponding Figures & Comparative Financial Statements	Comparative Information	01.04.2011
SA 720	The Auditor's Responsibilities Relating to Other Information	Other Information	01.04.2018
800 – 899	SPECIALISED AREAS		
SA 800	Special Considerations - Audits of Financial Statements Prepared in Accordance with Special Purpose Framework	Special Purpose Framework	01.04.2011
SA 805	Special Considerations - Audits of Single Financial Statements & Specific Elements, Accounts or Items of a Financial Statement	Single Financial Statement/ Specific Elements	01.04.2011
SA 810	Engagements to Report on Summary Financial Statements	Summary	01.04.2011
2000 – 2699	STANDARDS ON REVIEW ENGAGEMENTS (SRE)		
SRE 2400	Engagements to Review Historical Financial Statements	Review of Historical FS	01.04.2016
SRE 2410	Review of Interim Financial Information Performed by the Independent Auditor of the Entity	Review of Interim FI	01.04.2010
3000 – 3699	STANDARDS ON ASSURANCE ENGAGEMENTS (SAE)		
SAE 3400	The Examination of Prospective Financial Information	Examination	01.04.2007
SAE 3402	Assurance Report on Controls at a Service Organisation	Service Auditor	01.04.2011
SAE 3420	Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus	Pro Financial Information	01.04.2016
4000 – 4699	STANDARDS ON RELATED SERVICES (SRS)		
SRS 4400	Engagements to Perform Agreed-upon Procedures Regarding Financial Information	Agreed Upon Procedures	01.04.2004
SRS 4410	Compilation Engagements	Compilation	01.04.2016

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LIST OF IMPORTANT ABBREVIATIONS

AFRF (SA 200)	APPLICABLE FINANCIAL REPORTING FRAMEWORK
FRF	FINANCIAL REPORTING FRAMEWORK
GPF	GENERAL PURPOSE FRAMEWORK
SPF (SA 800)	SPECIAL PURPOSE FRAMEWORK
RMM (SA 200)	RISKS OF MATERIAL MISSTATEMENT

SAAE (SA 200)	SUFFICIENT APPROPRIATE AUDIT EVIDENCE
TCWG (SA 260)	THOSE CHARGED WITH GOVERNANCE
MGMT	MANAGEMENT
WR (SA 580)	WRITTEN REPRESENTATIONS
FI	FINANCIAL INFORMATION
HFI	HISTORICAL FINANCIAL INFORMATION
IFI (SRE 2410)	INTERIM FINANCIAL INFORMATION
PFI (SAE 3400)	PROSPECTIVE FINANCIAL INFORMATION
PFFI (SAE 3420)	PRO FORMA FINANCIAL INFORMATION
FS	FINANCIAL STATEMENTS
AFS	AUDITED FINANCIAL STATEMENTS
CFS	CONSOLIDATED FINANCIAL STATEMENTS
SFS (SA 810)	SUMMARY FINANCIAL STATEMENTS
SGFS	SINGLE FINANCIAL STATEMENT
CG	CENTRAL GOVERNMENT
NTE	NATURE, TIMING & EXTENT

3

IMPORTANT TERMS

1.	Historical financial information	<ul style="list-style-type: none"> Information expressed in financial terms in relation to a particular entity, derived primarily from that entity's accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.
2.	Financial Statements	<ul style="list-style-type: none"> A structured representation of historical financial information, including related notes, intended to communicate an entity's economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The related notes ordinarily comprise a summary of significant accounting policies & other explanatory information. The term "financial statements" ordinarily refers to a complete set of financial statements as determined by the requirements of the applicable financial reporting framework, but can also refer to a single financial statement.
3.	Applicable Financial Reporting Framework	<ul style="list-style-type: none"> The financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation & presentation of the financial statements that is acceptable in view of the nature of the entity & the objective of the financial statements, or that is required by law or regulation. The term "fair presentation framework" is used to refer to a financial reporting framework that requires compliance with the requirements of the framework &: <ul style="list-style-type: none"> (i) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or (ii) Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances. The term "compliance framework" is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (i) or (ii) above.
4.	Auditor	<ul style="list-style-type: none"> "Auditor" is used to refer to the person or persons conducting the audit, usually the engagement partner or other members of the engagement team, or, as applicable, the firm. Where an SA expressly intends that a requirement or responsibility be fulfilled by

		the engagement partner, the term “engagement partner” rather than “auditor” is used. “Engagement partner” & “firm” are to be read as referring to their public sector equivalents where relevant.
5.	Management	<ul style="list-style-type: none"> ➤ The person(s) with executive responsibility for the conduct of the entity’s operations. ➤ For some entities in some jurisdictions, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager.
6.	Those Charged With Governance	<ul style="list-style-type: none"> ➤ The person(s) or organisation(s) (e.g., a corporate trustee) with responsibility for overseeing the strategic direction of the entity & obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.
7.	Internal Control System	<ul style="list-style-type: none"> ➤ The process designed, implemented & maintained by those charged with governance, management & other personnel to provide reasonable assurance about the achievement of an entity’s objectives with regard to reliability of financial reporting, effectiveness & efficiency of operations, safeguarding of assets, & compliance with applicable laws & regulations. The term “controls” refers to any aspects of one or more of the components of internal control. ➤ "Internal Control System" means all the policies & procedures (internal controls) adopted by the management of an entity to assist in achieving management's objective of ensuring, as far as practicable, the orderly & efficient conduct of its business, including adherence to management policies, the safeguarding of assets, the prevention & detection of fraud & error, the accuracy & completeness of the accounting records, & the timely preparation of reliable financial information.
8.	Premise	<ul style="list-style-type: none"> ➤ Premise, relating to the responsibilities of management &, where appropriate, those charged with governance, on which an audit is conducted – That management &, where appropriate, those charged with governance have the following responsibilities that are fundamental to the conduct of an audit in accordance with SAs. That is, responsibility: <ul style="list-style-type: none"> (i) For the preparation & presentation of the financial statements in accordance with the applicable financial reporting framework; this includes the design, implementation & maintenance of internal control relevant to the preparation & presentation of financial statements that are free from material misstatement, whether due to fraud or error; & (ii) To provide the auditor with: <ul style="list-style-type: none"> (a) All information, such as records & documentation, & other matters that are relevant to the preparation & presentation of the financial statements; (b) Any additional information that the auditor may request from management &, where appropriate, those charged with governance; & (c) Unrestricted access to those within the entity from whom the auditor determines it necessary to obtain audit evidence. ➤ In the case of a fair presentation framework, the responsibility is for the preparation & fair presentation of the financial statements in accordance with the financial reporting framework; or the preparation of financial statements that give a true & fair view in accordance with the financial reporting framework. This applies to all references to “preparation & presentation of the financial statements” in the SAs. ➤ The “premise, relating to the responsibilities of management &, where appropriate, those charged with governance, on which an audit is conducted” may also be referred to as the “premise”.
9.		<ul style="list-style-type: none"> ➤ In conducting an audit of FS, the overall objectives of the auditor are: <ul style="list-style-type: none"> (a) To obtain reasonable assurance about whether the FS as a whole are free from

	Overall Objectives of the Auditor	<p>material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the FS are prepared, in all material respects, in accordance with an Applicable Financial Reporting Framework; &</p> <p>(b) To report on the FS, & communicate as required by the SAs, in accordance with the auditor's findings.</p>
10.	Reasonable assurance	<p>➤ In the context of an audit of financial statements, a high, but not absolute, level of assurance.</p>
11.	Professional judgment	<p>➤ The application of relevant training, knowledge & experience, within the context provided by auditing, accounting & ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.</p>
12.	Professional skepticism	<p>➤ An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, & a critical assessment of audit evidence.</p>
13.	Assertions	<p>➤ Representations by management, explicit or otherwise, that are embodied in the financial statements, as used by the auditor to consider the different types of potential misstatements that may occur.</p>
14.	Misstatement	<p>➤ A difference between the amount, classification, presentation, or disclosure of a reported financial statement item & the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework.</p> <p>➤ Misstatements can arise from error or fraud.</p> <p>➤ When the auditor expresses an opinion on whether the financial statements are presented fairly, in all material respects, or give a true & fair view, misstatements also include those adjustments of amounts, classifications, presentation, or disclosures that, in the auditor's judgment, are necessary for the financial statements to be presented fairly, in all material respects, or to give a true & fair view.</p>
15.	Business Risk	<p>➤ A risk resulting from significant conditions, events, circumstances, actions or inactions that could adversely affect an entity's ability to achieve its objectives & execute its strategies, or from the setting of inappropriate objectives & strategies.</p>
16.	Audit Risk	<p>➤ The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated.</p> <p>➤ Audit risk is a function of the risks of material misstatement & detection risk.</p>
17.	Risk of Material Misstatement	<p>➤ The risk that the financial statements are materially misstated prior to audit. This consists of two components, described as follows at the assertion level: Inherent Risk & Control Risk.</p>
18.	Significant Risk	<p>➤ An identified & assessed risk of material misstatement that, in the auditor's judgment, requires special audit consideration.</p>
19.	Inherent Risk	<p>➤ The susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.</p>
20.	Control Risk	<p>➤ The risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure & that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected & corrected, on a timely basis by the entity's internal control.</p>
21.	Detection Risk	<p>➤ The risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists & that could be material, either individually or when aggregated with other misstatements.</p>
22.	Audit Evidence	<p>➤ 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</p>

		<p>records underlying the financial statements & other information. For purposes of the SAs:</p> <p>(i) Sufficiency of audit evidence is the measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor's assessment of the risks of material misstatement & also by the quality of such audit evidence.</p> <p>(ii) Appropriateness of audit evidence is the measure of the quality of audit evidence; that is, its relevance & its reliability in providing support for the conclusions on which the auditor's opinion is based.</p>														
23.	<p>7 Methods of Obtaining Audit Evidence</p>	<table border="1"> <tr> <td>Inspection</td> <td> <p>➤ Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset.</p> </td> </tr> <tr> <td>External Confirmations</td> <td> <p>➤ An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium. (SA 505)</p> </td> </tr> <tr> <td>Analytical Procedures</td> <td> <p>➤ Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial & non-financial data. (SA 520)</p> </td> </tr> <tr> <td>Inquiry</td> <td> <p>➤ Inquiry consists of seeking information of knowledgeable persons, both financial & non-financial, within the entity or outside the entity. Inquiry is used extensively throughout the audit in addition to other audit procedures. Inquiries may range from formal written inquiries to informal oral inquiries. Evaluating responses to inquiries is an integral part of the inquiry process.</p> </td> </tr> <tr> <td>Observation</td> <td> <p>➤ Observation consists of looking at a process or procedure being performed by others, for eg., the auditor's observation of inventory counting by the entity's personnel, or of the performance of control activities.</p> </td> </tr> <tr> <td>Recalculation</td> <td> <p>➤ Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation may be performed manually or electronically.</p> </td> </tr> <tr> <td>Reperformance</td> <td> <p>➤ Re-performance involves the auditor's independent execution of procedures or controls that were performed as part of the entity's internal control.</p> </td> </tr> </table>	Inspection	<p>➤ Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset.</p>	External Confirmations	<p>➤ An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium. (SA 505)</p>	Analytical Procedures	<p>➤ Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial & non-financial data. (SA 520)</p>	Inquiry	<p>➤ Inquiry consists of seeking information of knowledgeable persons, both financial & non-financial, within the entity or outside the entity. Inquiry is used extensively throughout the audit in addition to other audit procedures. Inquiries may range from formal written inquiries to informal oral inquiries. Evaluating responses to inquiries is an integral part of the inquiry process.</p>	Observation	<p>➤ Observation consists of looking at a process or procedure being performed by others, for eg., the auditor's observation of inventory counting by the entity's personnel, or of the performance of control activities.</p>	Recalculation	<p>➤ Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation may be performed manually or electronically.</p>	Reperformance	<p>➤ Re-performance involves the auditor's independent execution of procedures or controls that were performed as part of the entity's internal control.</p>
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24.	<p>Risk Assessment Procedures</p>	<p>➤ The audit procedures performed to obtain an understanding of the entity & its environment, including the entity's internal control, to identify & assess the risks of material misstatement, whether due to fraud or error, at the financial statement & assertion levels.</p>														
25.	<p>Further Audit Procedures</p>	<p>➤ Further Audit Procedures comprise of:</p> <p>(i) Tests of controls, when required by the SAs or when the auditor has chosen to do so; &</p> <p>(ii) Substantive procedures, including tests of details & substantive analytical procedures.</p>														
26.	<p>Tests of Control</p>	<p>➤ An audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting & correcting, material misstatements at the assertion level.</p>														
27.	<p>Substantive Procedures</p>	<p>➤ An audit procedure designed to detect material misstatements at the assertion level. Substantive procedures comprise:</p> <p>(i) Tests of details (of classes of transactions, account balances, & disclosures), &</p> <p>(ii) Substantive analytical procedures.</p>														