

AU-C Section 300

Planning an Audit

Source: SAS No. 122; SAS No. 128.

Effective for audits of financial statements for periods ending on or after December 15, 2012.

Introduction

Scope of This Section

.01 This section addresses the auditor's responsibility to plan an audit of financial statements. This section is written in the context of recurring audits. Additional considerations in an initial audit engagement are separately identified in this section. Matters related to planning audits of group financial statements are addressed in section 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*. (Ref: par .A1–.A3)

The Role and Timing of Planning

.02 Planning an audit involves establishing the overall audit strategy for the engagement and developing an audit plan. Adequate planning benefits the audit of financial statements in several ways, including the following:

- Helping the auditor identify and devote appropriate attention to important areas of the audit
- Helping the auditor identify and resolve potential problems on a timely basis
- Helping the auditor properly organize and manage the audit engagement so that it is performed in an effective and efficient manner
- Assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks and allocating team member responsibilities
- Facilitating the direction and supervision of engagement team members and the review of their work
- Assisting, when applicable, in coordination of work done by auditors of components and specialists

Effective Date

.03 This section is effective for audits of financial statements for periods ending on or after December 15, 2012.

Objective

.04 The objective of the auditor is to plan the audit so that it will be performed in an effective manner.

Requirements

Involvement of Key Engagement Team Members

.05 The engagement partner and other key members of the engagement team should be involved in planning the audit, including planning and participating in the discussion among engagement team members. (Ref: par. .A4–.A5)

Preliminary Engagement Activities

.06 The auditor should undertake the following activities at the beginning of the current audit engagement:

- a. Performing procedures required by section 220, *Quality Control for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*, regarding the continuance of the client relationship and the specific audit engagement
- b. Evaluating compliance with relevant ethical requirements in accordance with section 220
- c. Establishing an understanding of the terms of the engagement as required by section 210, *Terms of Engagement* (Ref: par. .A6–.A8)

Planning Activities

.07 The auditor should establish an overall audit strategy that sets the scope, timing, and direction of the audit and that guides the development of the audit plan.

.08 In establishing the overall audit strategy, the auditor should

- a. identify the characteristics of the engagement that define its scope;
- b. ascertain the reporting objectives of the engagement in order to plan the timing of the audit and the nature of the communications required;
- c. consider the factors that, in the auditor's professional judgment, are significant in directing the engagement team's efforts;
- d. consider the results of preliminary engagement activities and, when applicable, whether knowledge gained on other engagements performed by the engagement partner for the entity is relevant; and
- e. ascertain the nature, timing, and extent of resources necessary to perform the engagement. (Ref: par. .A9–.A13)

.09 The auditor should develop an audit plan that includes a description of the following:

- a. The nature and extent of planned risk assessment procedures, as determined under section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*
- b. The nature, timing, and extent of planned further audit procedures at the relevant assertion level, as determined under section 330, *Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained*
- c. Other planned audit procedures that are required to be carried out so that the engagement complies with generally accepted auditing standards (Ref: par. .A14)

.10 The auditor should update and change the overall audit strategy and audit plan, as necessary, during the course of the audit. (Ref: par. .A15)

.11 The auditor should plan the nature, timing, and extent of direction and supervision of engagement team members and the review of their work. (Ref: par. .A16–.A17)

Determining the Extent of Involvement of Professionals Possessing Specialized Skills

.12 The auditor should consider whether specialized skills are needed in performing the audit. If specialized skills are needed, the auditor should seek the assistance of a professional possessing such skills, who either may be on the auditor's staff or an outside professional.¹ In such circumstances, the auditor should have sufficient knowledge to communicate the objectives of the other professional's work; evaluate whether the specified audit procedures will meet the auditor's objectives; and evaluate the results of the audit procedures applied as they relate to the nature, timing, and extent of further planned audit procedures. Section 620, *Using the Work of an Auditor's Specialist*, addresses the auditor's use of the work of specialists in an audit. (Ref: par. .A18–.A19)

Additional Considerations in Initial Audit Engagements

.13 The auditor should undertake the following activities prior to starting an initial audit:

- a. Performing procedures required by section 220
- b. Communicating with the predecessor auditor when there has been a change of auditors, in accordance with section 210² (Ref: par. .A20)

Documentation

.14 The auditor should include in the audit documentation the following:³

- a. The overall audit strategy
- b. The audit plan
- c. Any significant changes made during the audit engagement to the overall audit strategy or the audit plan and the reasons for such changes (Ref: par. .A21–.A24)

Application and Other Explanatory Material

The Role and Timing of Planning (Ref: par. .01)

.A1 The nature and extent of planning activities will vary according to the size and complexity of the entity, the key engagement team members' previous experience with the entity, and changes in circumstances that occur during the audit engagement.

¹ Paragraph .16 of section 220, *Quality Control for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*.

² Paragraph .11 of section 210, *Terms of Engagement*.

³ Paragraphs .08–.12 and .A8 of section 230, *Audit Documentation*.

.A2 Planning is not a discrete phase of an audit but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement. Planning, however, includes consideration of the timing of certain activities and audit procedures that need to be completed prior to the performance of further audit procedures. For example, planning includes the need to consider, prior to the auditor's identification and assessment of the risks of material misstatement, such matters as the following:

- The analytical procedures to be applied as risk assessment procedures
- A general understanding of the legal and regulatory framework applicable to the entity and how the entity is complying with that framework
- The determination of materiality
- The involvement of specialists
- The performance of other risk assessment procedures

.A3 The auditor may decide to discuss elements of planning with the entity's management to facilitate the conduct and management of the audit engagement (for example, to coordinate some of the planned audit procedures with the work of the entity's personnel). Although these discussions often occur, the overall audit strategy and the audit plan remain the auditor's responsibility. When discussing matters included in the overall audit strategy or audit plan, care is required in order not to compromise the effectiveness of the audit. For example, discussing the nature and timing of detailed audit procedures with management may compromise the effectiveness of the audit by making the audit procedures too predictable.

Involvement of Key Engagement Team Members (Ref: par. .05)

.A4 The involvement of the engagement partner and other key members of the engagement team in planning the audit draws on their experience and insight, thereby enhancing the effectiveness and efficiency of the planning process. The engagement partner may delegate portions of the planning and supervision of the audit to other firm personnel.

.A5 Section 315 requires a discussion among the audit team about the susceptibility of the entity's financial statements to material misstatement.⁴ This discussion also may include the discussion regarding the risks of material misstatement due to fraud, as required by section 240, *Consideration of Fraud in a Financial Statement Audit*.⁵ The objective of this discussion is for members of the audit team to gain a better understanding of the potential for material misstatements of the financial statements resulting from fraud or error in the specific areas assigned to them and to understand how the results of the audit procedures that they perform may affect other aspects of the audit, including the decisions about the nature, timing, and extent of further audit procedures.

Preliminary Engagement Activities (Ref: par. .06)

.A6 Performing the preliminary engagement activities, which are specified in paragraph .06, at the beginning of the current audit engagement assists

⁴ Paragraph .11 of section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*.

⁵ Paragraph .15 of section 240, *Consideration of Fraud in a Financial Statement Audit*.

the auditor in identifying and evaluating events or circumstances that may adversely affect the auditor's ability to plan and perform the audit engagement.

.A7 Performing these preliminary engagement activities enables the auditor to plan an audit engagement for which, for example

- the auditor maintains the necessary independence and ability to perform the engagement.
- the auditor has no issues with management integrity that may affect the auditor's willingness to continue the engagement.
- the auditor has no misunderstanding with the entity about the terms of the engagement.

.A8 The auditor's consideration of client continuance and relevant ethical requirements, including independence, occurs throughout the audit engagement as conditions and changes in circumstances occur. Performing initial procedures on both client continuance and evaluation of relevant ethical requirements (including independence) at the beginning of the current audit engagement means that they are completed prior to the performance of other significant activities for the current audit engagement. For continuing audit engagements, such initial procedures often begin shortly after (or in connection with) the completion of the previous audit.

Planning Activities

The Overall Audit Strategy (Ref: par. .07–.08)

.A9 The process of establishing the overall audit strategy assists the auditor to determine, subject to the completion of the auditor's risk assessment procedures, such matters as the following:

- The resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas or the involvement of specialists on complex matters
- The amount of resources to allocate to specific audit areas, such as the number of team members assigned to observe the inventory count at material locations, the extent of review of component auditors' work in the case of group audits, or the audit budget (in hours) to allocate to high risk areas
- When these resources are to be deployed, such as whether at an interim audit stage or at key cut-off dates
- How such resources are managed, directed, and supervised, such as when team briefing and debriefing meetings are expected to be held, how the engagement partner and manager reviews are expected to take place (for example, on site or off site), and whether to complete engagement quality control reviews

.A10 The appendix, "Considerations in Establishing the Overall Audit Strategy," lists examples of considerations in establishing the overall audit strategy.

.A11 Once the overall audit strategy has been established, an audit plan can be developed to address the various matters identified in the overall audit strategy, taking into account the need to achieve the audit objectives through the efficient use of the auditor's resources. The establishment of the overall audit strategy and the detailed audit plan are not necessarily discrete or

sequential processes but are closely interrelated because changes in one may result in consequential changes to the other.

Considerations Specific to Smaller, Less Complex Entities

.A12 In audits of smaller entities, the entire audit may be conducted by a very small audit team. Many audits of smaller entities involve the engagement partner (who may be a sole practitioner) working with one engagement team member (or without any engagement team members). With a smaller team, coordination of, and communication between, team members is easier. Establishing the overall audit strategy for the audit of a smaller entity need not be a complex or time consuming exercise; it varies according to the size and complexity of the entity, the complexity of the audit, and the size of the engagement team. For example, a brief memorandum prepared at the completion of the previous audit, based on a review of the working papers and highlighting issues identified in the audit just completed, updated in the current period, based on discussions with the owner-manager, can serve as the documented audit strategy for the current audit engagement if it covers the matters noted in paragraph .07.

Communications With Those Charged With Governance

.A13 Section 260, *The Auditor's Communication With Those Charged With Governance*, requires the auditor to communicate with those charged with governance an overview of the planned scope and timing of the audit.⁶

The Audit Plan (Ref: par. .09)

.A14 The audit plan is more detailed than the overall audit strategy in that it includes the nature, timing, and extent of audit procedures to be performed by engagement team members. Planning for these audit procedures takes place over the course of the audit as the audit plan for the engagement develops. For example, planning of the auditor's risk assessment procedures occurs early in the audit process. However, planning the nature, timing, and extent of specific further audit procedures depends on the outcome of those risk assessment procedures. In addition, the auditor may begin the execution of further audit procedures for some classes of transactions, account balances, and disclosures before planning all remaining further audit procedures.

Changes to Planning Decisions During the Course of the Audit (Ref: par. .10)

.A15 As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan and, thereby, the resulting planned nature, timing, and extent of further audit procedures, based on the revised consideration of assessed risks. This may be the case when information comes to the auditor's attention that differs significantly from the information available when the auditor planned the audit procedures. For example, audit evidence obtained through the performance of substantive procedures may contradict the audit evidence obtained through tests of controls.

Direction, Supervision, and Review (Ref: par. .11)

.A16 The nature, timing, and extent of the direction and supervision of engagement team members and review of their work vary, depending on many factors, including the following:

- The size and complexity of the entity

⁶ Paragraph .11 of section 260, *The Auditor's Communication With Those Charged With Governance*.

- The area of the audit
- The assessed risks of material misstatement (for example, an increase in the assessed risk of material misstatement for a given area of the audit ordinarily requires a corresponding increase in the extent and timeliness of direction and supervision of engagement team members and a more detailed review of their work)
- The capabilities and competence of the individual team members performing the audit work

Section 220 contains further guidance on the direction, supervision, and review of audit work.

Considerations Specific to Smaller, Less Complex Entities

.A17 If an audit is carried out entirely by the engagement partner, questions of direction and supervision of engagement team members and review of their work do not arise. In such cases, the engagement partner, having personally conducted all aspects of the work, will be aware of all material issues. Forming an objective view on the appropriateness of the judgments made in the course of the audit can present practical problems when the same individual also performs the entire audit. If particularly complex or unusual issues are involved and the audit is performed by a sole practitioner, it may be desirable to consult with other suitably experienced auditors or the auditor's professional body.

Determining the Extent of Involvement of Professionals Possessing Specialized Skills (Ref: par. .12)

.A18 An auditor may decide to seek the assistance of a professional with specialized skills necessary to complete various aspects of the engagement. These professionals may include valuation experts, appraisers, actuaries, tax specialists, and IT professionals. For example, the use of professionals possessing IT skills to determine the effect of IT on the audit, understand the IT controls, or design and perform tests of IT controls or substantive procedures is a significant aspect of many audit engagements. In determining whether such a professional is needed on the audit team, the auditor may consider such factors as the following:

- The complexity of the entity's systems and IT controls and the manner in which they are used in conducting the entity's business
- The significance of changes made to existing systems or the implementation of new systems
- The extent to which data is shared among systems
- The extent of the entity's participation in electronic commerce
- The entity's use of emerging technologies
- The significance of audit evidence that is available only in electronic form

.A19 Audit procedures that the auditor may assign to a professional possessing IT skills include inquiring of an entity's IT personnel how data and transactions are initiated, authorized, recorded, processed, and reported and how IT controls are designed; inspecting systems documentation; observing the operation of IT controls; and planning and performing tests of IT controls.

Additional Considerations in Initial Audit Engagements (Ref: par. .13)

.A20 The purpose and objective of planning the audit are the same whether the audit is an initial or recurring engagement. However, for an initial audit, the auditor may need to expand the planning activities because the auditor does not ordinarily have the previous experience with the entity that is considered when planning recurring engagements. For an initial audit engagement, additional matters the auditor may consider in establishing the overall audit strategy and audit plan include the following:

- Arrangements to be made with the predecessor auditor (for example, to review the predecessor auditor's working papers [see section 510, *Opening Balances—Initial Audit Engagements, Including Reaudit Engagements*])⁷
- Any major issues (including the application of accounting principles or auditing and reporting standards) discussed with management in connection with the initial selection as auditor, the communication of these matters to those charged with governance, and how these matters affect the overall audit strategy and audit plan
- The audit procedures necessary to obtain sufficient appropriate audit evidence regarding opening balances (see section 510)⁸
- Other procedures required by the firm's system of quality control for initial audit engagements (for example, the firm's system of quality control may require the involvement of another partner or senior individual to review the overall audit strategy prior to commencing significant audit procedures or to review reports prior to their issuance)

Documentation (Ref: par. .14)

.A21 The documentation of the overall audit strategy is a record of the key decisions considered necessary to properly plan the audit and communicate significant issues to the engagement team. For example, the auditor may summarize the overall audit strategy in the form of a memorandum that contains key decisions regarding the overall scope, timing, and conduct of the audit.

.A22 The documentation of the audit plan is a record of the planned nature, timing, and extent of risk assessment procedures and further audit procedures at the relevant assertion level in response to the assessed risks. It also serves as a record of the proper planning of the audit procedures that can be reviewed and approved prior to their performance. The auditor may use standard audit programs or audit completion checklists, tailored as needed to reflect the particular engagement circumstances.

.A23 A record of the significant changes to the overall audit strategy and the audit plan and resulting changes to the planned nature, timing, and extent of audit procedures explain why the significant changes were made and why the overall strategy and audit plan were finally adopted for the audit. It also reflects the appropriate response to the significant changes occurring during the audit.

⁷ Paragraphs .07 and .A2–.A11 of section 510, *Opening Balances—Initial Audit Engagements, Including Reaudit Engagements*.

⁸ Paragraph .08 of section 510.

Considerations Specific to Smaller, Less Complex Entities

.A24 As discussed in paragraph .A12, a suitable, brief memorandum may serve as the documented strategy for the audit of a smaller entity. For the audit plan, standard audit programs or checklists (see paragraph .A22) drawn up on the assumption of few relevant control activities, which is likely to be the case in a smaller entity, may be used, provided that they are tailored to the circumstances of the engagement, including the auditor's risk assessments.

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Appendix—Considerations in Establishing the Overall Audit Strategy (Ref: par. .07–.08 and .A9–.A12)

This appendix provides examples of matters the auditor may consider in establishing the overall audit strategy. Many of these matters also will influence the auditor's detailed audit plan. The examples provided cover a broad range of matters applicable to many engagements. Although some of the following matters may be required by other AU-C sections, not all matters are relevant to every audit engagement, and the list is not necessarily complete.

Characteristics of the Engagement

The following are some examples of characteristics of the engagement:

- The financial reporting framework on which the financial information to be audited has been prepared, including any need for reconciliations to another financial reporting framework
- Industry specific reporting requirements, such as reports mandated by industry regulators
- The expected audit coverage, including the number and locations of components to be included
- The nature of the control relationships between a parent and its components that determine how the group is to be consolidated
- The extent to which components are audited by other auditors
- The nature of the business divisions to be audited, including the need for specialized knowledge
- The reporting currency to be used, including any need for currency translation for the audited financial information
- The need for statutory or regulatory audit requirements (for example, the Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*)
- Whether the entity has an internal audit function and, if so, whether (in which areas and to what extent) the work of the internal audit function can be used in obtaining audit evidence or whether internal auditors can be used to provide direct assistance
- The entity's use of service organizations and how the auditor may obtain evidence concerning the design or operation of controls performed by them
- The expected use of audit evidence obtained in previous audits (for example, audit evidence related to risk assessment procedures and tests of controls)
- The effect of IT on the audit procedures, including the availability of data and the expected use of computer assisted audit techniques
- The coordination of the expected coverage and timing of the audit work with any reviews of interim financial information and the effect on the audit of the information obtained during such reviews
- The availability of client personnel and data

Reporting Objectives, Timing of the Audit, and Nature of Communications

The following examples illustrate reporting objectives, timing of the audit, and nature of communications:

- The entity's timetable for reporting, including interim periods
- The organization of meetings with management and those charged with governance to discuss the nature, timing, and extent of the audit work
- The discussion with management and those charged with governance regarding the expected type and timing of reports to be issued and other communications, both written and oral, including the auditor's report, management letters, and communications to those charged with governance
- The discussion with management regarding the expected communications on the status of audit work throughout the engagement
- Communication with auditors of components regarding the expected types and timing of reports to be issued and other communications in connection with the audit of components
- The expected nature and timing of communications among engagement team members, including the nature and timing of team meetings and timing of the review of work performed
- Whether there are any other expected communications with third parties, including any statutory or contractual reporting responsibilities arising from the audit

Significant Factors, Preliminary Engagement Activities, and Knowledge Gained on Other Engagements

The following examples illustrate significant factors, preliminary engagement activities, and knowledge gained on other engagements:

- The determination of materiality, in accordance with section 320, *Materiality in Planning and Performing an Audit*, and, when applicable, the following:
 - The determination of materiality for components and communication thereof to component auditors in accordance with section 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*
 - The preliminary identification of significant components and material classes of transactions, account balances, and disclosures
- Preliminary identification of areas in which there may be a higher risk of material misstatement
- The effect of the assessed risk of material misstatement at the overall financial statement level on direction, supervision, and review
- The manner in which the auditor emphasizes to engagement team members the need to maintain a questioning mind and exercise

professional skepticism in gathering and evaluating audit evidence

- Results of previous audits that involved evaluating the operating effectiveness of internal control, including the nature of identified deficiencies and action taken to address them
- The discussion of matters that may affect the audit with firm personnel responsible for performing other services to the entity
- Evidence of management's commitment to the design, implementation, and maintenance of sound internal control, including evidence of appropriate documentation of such internal control
- Volume of transactions, which may determine whether it is more efficient for the auditor to rely on internal control
- Importance attached to internal control throughout the entity to the successful operation of the business
- Significant business developments affecting the entity, including changes in IT and business processes; changes in key management; and acquisitions, mergers, and divestments
- Significant industry developments, such as changes in industry regulations and new reporting requirements
- Significant changes in the financial reporting framework, such as changes in accounting standards
- Other significant relevant developments, such as changes in the legal environment affecting the entity

Nature, Timing, and Extent of Resources

The following examples illustrate the nature, timing, and extent of resources:

- The selection of the engagement team (including, when necessary, the engagement quality control reviewer [see section 220, *Quality Control for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*]) and the assignment of audit work to the team members, including the assignment of appropriately experienced team members to areas in which there may be higher risks of material misstatement
- Engagement budgeting, including considering the appropriate amount of time to set aside for areas in which there may be higher risks of material misstatement

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