

Workshop on Creating a Better Financial Reporting Ecosystem

Risk of Material Misstatement

CA Milan Mody



NFRA in collaboration with ICAI:
Centre for Audit Quality Committee of ICAI
& Pune Branch of WIRC

Friday, 19 June 2026

Session Plan

- | | | | |
|----------|--|--|---------------|
| 1 | The framework SA 315 & 330 | Risk to response journey ·
Audit procedures | 15 min |
| 2 | Case studies | 11 examples / scenarios | 30 min |
| 3 | Key Learnings from NFRA & QRB | Outcome of review · Key points | 10 min |
| 4 | Practical tips & wrap-up | Roadmap · Risk register ·
Takeaways · Q&A | 5 min |

Setting the Context

Why risk assessment deserves the profession's attention



Businesses are more complex



Reporting is more judgmental



Technology has changed the audit



Trust is the product

The opportunity: A sharp, entity-specific risk assessment turns audit effort into real assurance by focusing attention on where misstatements can arise, clearly demonstrating audit value.

- ✓ **Quality and efficiency together:** Well-assessed risk concentrates effort where it matters and avoids unnecessary work
- ✓ **Lessons worth keeping:** Major failures stem from incentives, structures, and estimates—not arithmetic.
- ✓ **The lever we control:** Detection risk can be calibrated only through a robust ROMM assessment.

Why RoMM Drives the Entire Audit

Audit Risk is a function of Risk of Material Misstatement & Detection Risk

where RoMM consists of Inherent Risk & Control Risk



Sets the direction

RoMM assessment determines the nature, timing & extent of further audit procedures (SA 330).



RoMM is the entity's risk

It exists independently of the audit. The auditor assesses it. (detection risk within the auditor's control).



Risk assessment is the foundation of audit

- Audit strategy is based on identified risks
- Incorrect RoMM assessment can result in insufficient audit evidence.
- Deficiencies in RoMM often lead to deficiencies throughout the audit.

Nature of Risk

Risk Type	Meaning	RoMM not addressed
Inherent	Susceptibility of an assertion to misstatement before considering controls.	Goodwill impairment testing, new ERP system implemented, derivative contracts valuation, revenue recognition at year end.
Control	Risk that the entity's controls fail to prevent or detect a misstatement.	Revenue recognition cut-off control failure, BRS control not operating effectively.
Detection	Risk that audit procedures fail to detect an existing material misstatement.	Auditor performs limited testing of ECL models and does not challenge key assumptions.
Significant	RoMM requiring special audit consideration due to complexity, judgment, estimation, fraud risk, etc.	Management overlay in ECL provision without proper rationale, robust support, not adequately documented.

The Required Understanding

SA 315, Para 11-24 — what you must know before assessing risk

-  **Nature of the entity**
Operations, ownership, governance, structure, financing, investments.
-  **Industry, regulatory & external factors**
Competitive landscape, regulation, economic conditions, inputs obtained from previous auditor.
-  **Objectives, strategies & business risks**
Business risks that may translate into RoMM.
-  **Measurement & review of performance**
KPIs and incentives create pressure that can motivate misstatements such as inflated sales booking.
-  **Internal control**
Understand the control environment, risk assessment process, information systems, ERP environment, relevant control activities and its monitoring.

RoMM Operates at Two Levels

SA 315, Para 25 — both must be assessed



Financial Statement Level

- Pervasive — affects FS as a whole and many assertions
- Often from weak control environment, management integrity concerns, going-concern pressure
- Closely linked to fraud risk, E.g. management override
- Requires overall responses — team experience, supervision, unpredictability



Assertion Level

- Specific to classes of transactions, account balances and disclosures
- Identified for each relevant assertion — for example, existence of inventory, valuation of receivables
- Directly drives nature, timing and extent of tests of controls and substantive procedures
- Assessment may change as evidence is obtained

Risk Assessment Procedures

SA 315, Para 5–10



Inquiries

Management, internal audit, and others. Vary your sources; the CFO alone is not enough.



Analytical Procedures

Opening trial balance review, materiality setting, and trend/ratio analysis during planning.



Observation & Inspection

Plant visits, walkthroughs, minutes, contracts, MIS reports, Legal cases. Contradicts what management tells you.



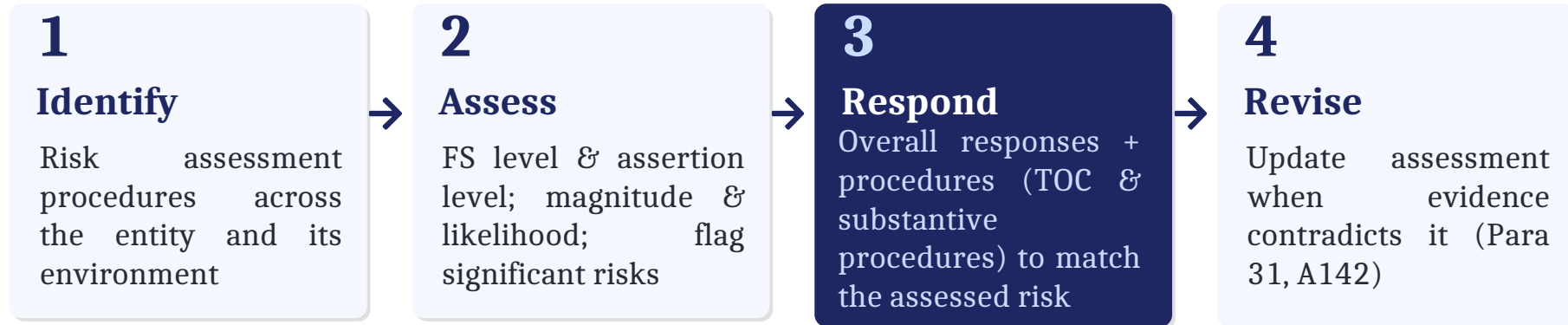
Engagement team discussion — non-negotiable. Partner and key members must discuss susceptibility of the FS to misstatement, including fraud. In practice, hold it before fieldwork & minute it, share with members not present.

Conditions & Events Indicating RoMM

SA 315, Appendix 2 — use as a planning checklist

- Operations in economically unstable regions / markets
- Going concern and liquidity issues
- Constraints on availability of capital and credit
- New products, new lines of business, new locations
- Large acquisitions, reorganisations or unusual events
- Complex alliances, JVs and off-balance-sheet structures
- Significant related party transactions
- Lack of personnel with accounting / reporting skills
- Departure of key executives and finance staff
- Control deficiencies not addressed by management
- Changes in IT environment or systems implementation
- Litigation, contingent liabilities, prior period items

From Risk to Response



The auditor shall design and implement overall responses to address the assessed RoMM at the financial statement level by planning

- Nature— more reliable, externally sourced evidence; more unpredictability in procedures
- Timing — shift procedures from interim to period-end; surprise counts where manipulation risk exists
- Extent— larger samples, lower performance materiality (SA 320), more locations covered


Case Studies


Applying SA 315 judgement to practical scenarios

For each: what is the risk · at which level · is it significant · what response does SA 330 demand


Case 1 - Over-Time Revenue in an EPC Contract


Business Facts

 Listed EPC contractor executing multiple large infrastructure projects

 Several projects are in different stages of execution across locations

 Project plans and commercial terms were updated during the year

 Management performs periodic reviews of project performance and profitability

 The company has significant borrowings from lenders

RoMM identified

Inherent Risk:

- Judgment in project revenue recognition (significant risk)
- Estimation of project costs and profitability
- Changes in project plans and commercial arrangements

Control Risk: Reliance on project review and monitoring controls

Assertions impacted: Occurrence, cutoff, accuracy, valuations, completeness

Assessment & audit response (SA 330)

- Recalculate project stage of completion
- Challenge cost estimates and forecasts
- Test significant project changes
- Contract-to-revenue testing and unbilled revenue testing


Case 2 - Revenue from Sale of products


ROMMs		Inherent Risk	Control Risk		Fraud Risk	Overall ROMM
Sl.#	ROMM Description		Manual Controls	IT Environment		
ROMM 1	Revenue is recognised for arrangements that do not meet the definition of a contract under the standard or do not exist. (Ind AS 115)	Medium (M)	Low (L)	NA	No	Low (L)
ROMM 2	Revenue is not accurately recorded because the transaction price is not appropriately determined as per Ind AS 115	Significant (S)	NA	Low (L)	Yes	Significant (S)
ROMM 3	For performance obligations satisfied at a point in time, an inaccurate amount is recorded for revenue.	Medium (M)	NA	NA	No	Low (L)
ROMM 4	For performance obligations satisfied at a point in time, revenue is not recognised in the correct accounting period.	Significant (S)	High (H)	Low (L)	Yes	Significant (S)


Case 3 - Mid-Year ERP Migration

Business Facts

 Company implemented a new SAP S/4HANA ERP system during the year

 Revenue, inventory costing, procurement, and financial reporting processes are now highly automated

 Historical data, master data, and open transactions were migrated to the new system

 Business and finance teams were extensively involved in the implementation and go-live process

 Year-end financial reporting was completed using the new ERP environment

RoMM identified

Inherent Risk:

- Completeness and accuracy of migrated data
- Reliance on automated processing and reports
- Financial reporting through a new ERP environment (significant risk)

Control Risk: Ineffective ITGCs and automated controls


Assertions impacted: Occurrence, accuracy, valuations, completeness, presentation and disclosure


Assessment & audit response (SA 330)


- Test data migration accuracy
- Evaluate ITGC effectiveness
- Test key automated controls
- Validate system-generated reports


Case 4 - ECL in an NBFC Loan Book


Business Facts

 Mid-size NBFC with a significant wholesale real-estate loan portfolio

 Several large borrower accounts were restructured during the year

 Credit exposure is concentrated in a limited number of borrowers

 Management performed the year-end credit impairment assessment using historical and forward-looking information

 Senior management was closely involved in the impairment review process

RoMM identified

Inherent Risk:

- Concentrated exposure to large borrowers
- Restructured loan exposures
- Significant judgment in ECL estimation (significant risk)

Control Risk: Impairment review controls may not identify all credit deterioration indicators


Assertions impacted: Occurrence, accuracy, valuations, completeness, presentation and disclosure


Assessment & audit response (SA 330)

- Test ECL assumptions and data
- Review restructured exposures
- Assess borrower credit quality
- Evaluate ECL disclosures


Case 5 — Promoter Group & Related Parties


Business Facts

 Family-promoted auto-component group with operations across multiple entities

 A significant volume of sales was recorded with a customer added during the year, particularly in the last quarter

 The group entered into several transactions with entities operating in different business sectors

 Certain transactions involved movement of funds between entities within the wider group structure

 Members of the promoter family hold ownership and management positions across various group entities

RoMM identified

Inherent Risk:

- Revenue recognition from significant new customer relationships
- Substance and business rationale of group transactions
- Complex related party relationships and transactions

Control Risk: Inadequate identification and monitoring of related party transactions

Significant Risk: Unusual RPT


Assertions impacted: Occurrence, accuracy, valuations, completeness, presentation and disclosure


Assessment & audit response (SA 330)


- Identify and evaluate related party relationships
- Test significant and unusual transactions
- Assess business rationale and substance
- Review approvals and related disclosures

Case 6 - Fraud / Management override of controls


Business Facts


 **Industry:** Manufacturing (Listed Company)


 Revenue growth of **20%** despite an industry-wide slowdown

 Annual earnings targets achieved

 **30% of annual sales** recorded in the last month of the year

 Inventory increased by **25%** compared to the previous year

 Certain senior finance personnel have administrator access to the ERP system

 A significant portion of management compensation is linked to EBITDA and profit targets

RoMM identified

Inherent Risk:

- Revenue growth inconsistent with industry trends
- Significant year-end sales concentration
- Inventory growth amid slowing market conditions

Control Risk: Elevated risk from privileged ERP access

Significant Risk: Revenue recognition susceptible to management bias and fraud

Assertions impacted: Occurrence, cut off, accuracy, valuations, presentation and disclosure

Assessment & audit response (SA 330)

- Test revenue recognition and cut-off
- Assess inventory valuation (NRV)
- Review ERP access and override controls
- Test unusual journal entries and management bias

Case 7 – Impairment of investments

Business Facts

- 🏢 Company has significant investments in subsidiaries, associates, joint ventures, and other financial assets
- 🌐 The group operates across multiple industries and geographic markets
- 📈 Certain investees are in expansion and growth phases, while others are in mature business segments
- 🔄 During the year, some investees undertook restructuring initiatives and strategic business changes
- 📄 Updated business plans and long-term forecasts were prepared by management during the year
- 📅 Management performed its annual review of investment carrying values before finalization of the financial statements

RoMM identified

Inherent Risk:

- Valuation dependent on forecasts and assumptions
- Estimation uncertainty from business and strategic changes
- Complex assessment across investees and geographies

Control Risk: Reliance on management's valuation review process

Significant Risk: Material investments involving significant judgment

Assertions impacted: Valuation, accuracy, completeness, presentation and disclosure

Assessment & audit response (SA 330)

- Evaluate impairment indicators
- Challenge key assumptions & test valuation models
- Benchmark forecasts
- Use valuation specialists
- Test impairment & disclosures

Case 8 & 9 - Other ROMM in audit of FS

Area	Key RoMM	Areas	Audit response
Pre & Post IPO period	Management bias, aggressive reporting, disclosure risks	<ul style="list-style-type: none"> • Errors in Financial statement restatements • Preponement of revenue • IPO fund utilization – classification of end use 	<ul style="list-style-type: none"> • Heightened skepticism • detailed testing of revenue • external utilisation certificates by operating agencies
Level 3 fair valuations	High estimation uncertainty and use of unobservable inputs	<ul style="list-style-type: none"> • Overstatement of FV • Unreasonable assumptions used in valuation models • Inadequate disclosure of significant unobservable inputs 	<ul style="list-style-type: none"> • Challenge assumptions, • test valuation models • involve valuation specialists

Case 10 & 11 - Other ROMM in audit of FS

Area	Key RoMM	Areas	Audit response
Consolidation of financial statements	Incomplete component coverage, consolidation errors, group reporting risks	<ul style="list-style-type: none"> • Component coverage gaps • Inadequate evaluation of component risks • Consolidation and elimination errors • Acquisition and foreign currency translation errors 	<ul style="list-style-type: none"> • Assess significant components • Oversee component auditors • Evaluate component audit evidence • Test consolidation process
Foreign Currency Exposure & Geopolitical Supply-Chain Risks	Significant Forex exposures, supply-chain disruptions, Liquidity pressure & demand uncertainty	<ul style="list-style-type: none"> • Forex valuation errors • hedge accounting errors • country risk exposure • Risk of incomplete disclosures 	<ul style="list-style-type: none"> • Challenge assumptions • Recalculate forex gains/losses • assess operational impact • review disclosures

Key learnings from NFRA & QRB

Key learnings from NFRA

✘ Copy-paste risk assessment

Prior-year risk register rolled forward without testing whether changes have occurred (Para 9). Industry shifts, new ERP, new management — all ignored.

✘ Generic, entity-agnostic risks

"Revenue may be overstated" on every file. Risks not related to what can go wrong at the assertion level for this entity's transactions.

✘ No linkage to procedures

Risk register and audit programme live in separate worlds — procedures don't change even when assessed risk does. SA 330 linkage is the first thing reviewers test.

✘ Internal control understood on paper only

Walkthroughs not actually performed; design and implementation of controls never evaluated. Inquiry alone is not sufficient (A74).

Key learnings from QRB

✘ **Planning risks ≠ communicated risks**

Risks assessed at planning (e.g. revenue, inventory, override) differ from the risks presented to the Board — and the mitigating procedures for identified risks are not captured at all.

✘ **Revenue presumption unevaluated**

No evaluation of which revenue streams, transactions or assertions carry the SA 240 fraud risk; where the presumption is rebutted, the Para 47 documentation of reasons is missing.

✘ **TCWG communication informal**

Findings conveyed orally with no record, draft letters left unsigned, or the 'Board presentation' sent to GM-Finance rather than those charged with governance (SA 260).

✘ **Generic tools, thin documentation**

Standard checklists not designed in detail, no formal audit manual; IT/SAP risk reviewed through a generic checklist without assessing implementation and access risk.

Other key points

✘ Revenue fraud presumption rebutted casually

SA 240 presumption set aside with one line, no documented rationale for which revenue streams and why.

✘ Team discussion not held or not documented

Para 10 discussion treated as a formality; fraud susceptibility never genuinely brainstormed; no record of who attended and what was decided.

✘ Risk assessment never revised

Misstatements found during fieldwork exceed expectations, controls fail testing — yet the original assessment stands unchanged (Para 31).

✘ Documentation gaps (Para 32)

Sources of understanding, the discussion, identified risks and evaluated controls not traceable in the file. If it isn't documented, it wasn't done.

Practical tips







- 1 Pre-engagement** Carry forward acceptance/continuance insights; update prior-year knowledge for changes; preliminary analytics on draft numbers.
- 2 Planning** Team discussion with fraud lens; structured understanding (Appendix 2 checklist); walkthroughs of significant processes; set materiality.
- 3 Risk register** One register per engagement: risk → assertion → magnitude/likelihood → significant? → control reliance → planned response. Link each line to a programme step.
- 4 Execution** Perform responses; revise assessment when evidence contradicts it; accumulate misstatements and reconsider risk.
- 5 Completion** Final analytics; confirm assessment still supports the opinion; communicate significant risks and deficiencies; archive documentation.

The Working Tool: Risk Register

Illustrative entries — one row per identified risk

Identified risk	Account Assertion /	IR & CR RoMM	Significant?	Planned response
Cut-off manipulation near year-end to meet covenant targets	Revenue: occurrence, cut-off	High & High High	Yes	Test sales ±15 days of year-end to dispatch evidence; JE testing on revenue accounts; no interim reliance
ECL on trade receivables — high estimation uncertainty	Receivables: valuation	High & Medium High	Yes	Evaluate model & assumptions; independent re-performance; subsequent collections review
Inventory obsolescence in slow-moving SKUs	Inventory: valuation, existence	Medium & Medium Medium	No	Attend count; ageing analysis; NRV testing on sample of slow-moving items

Key Takeaways

-  RoMM assessment is engine of the audit - every procedure should trace back to an assessed risk.
-  Assess at both levels: pervasive FS-level risks demand overall responses; assertion-level risks shape specific procedures.
-  Higher ROMM requires stronger audit procedures
-  Treat significant risks — including the SA 240 presumptions — with the special consideration the standard demands.
-  Risk assessment is continuous: revise it when evidence contradicts it, and document the revision.
-  Implementation: traceability: understanding → risk register → audit programme → evidence → opinion.



Thank you
Any Questions