

Auditing Property, Plant and Equipment

The ultimate cheat sheet for external auditors testing property, plant and equipment in small and medium-sized organizations.

- Engagement Type: External Audit
- Client Industry: General Commercial
- Standards: US GAAS/ISA
- Area: Risk Assessment/Response to Risk

Risk Assessment



Typical Risks

Risk	Risk Level	Assertions
Depreciation charge may be incorrect	Normal	VA
Significant asset additions occurred	Normal	E, RO, VA
Significant asset disposals occurred	Normal	RO, C
Impact of repairs & maintenance costs	Normal	C
Impairment indicators exist	Normal	VA

Other Potential Risks

Legend: E = Existence, C = Completeness, RO = Rights & Obligations, VA = Valuation & Allocation

Risk	Assertions
Fully amortized assets are not used anymore	E, VA
Asset useful lives are not appropriate	VA
Impact of assets held at fair value	VA
Revaluation of assets performed in the period	VA
Impact of assets held for sale	RO, VA
Capitalization of borrowing costs	VA
Impact of assets in the course of construction	E, RO, VA
Impact of assets purchased with grants	VA
Impaired physical condition or asset may not exist	E, VA

Ratio Analysis



Typical Ratios

Ratio	Calculation
Depreciation	Depreciation Costs / PP&E
Growth in Non-Current Assets	(CY Non-Current Assets - PY Non-Current Assets) / PY Non-Current Assets
Growth in PP&E	(Closing PP&E - Opening PP&E) / Opening PP&E
Income / Non-Current Assets	Income / Non-Current Assets
Income / PP&E	Income / PP&E

Top Tips



- Testing significant PP&E additions and disposals are effective tests to commence at planning or interim.
- The depreciation charge is often recalculated as: (cost - salvage value) / estimated useful life of asset.
- Assets with a Net Book Value of zero should be removed from this calculation, where significant.
- If risk assessment has concluded that the entity is more likely to wish to overstate profits, the Completeness assertion may be deemed not relevant to PP&E.
- This can remove needing to review repairs & maintenance.
- Consider the need to remove assets with zero NBV from disclosure notes.
- Check PP&E physical condition and existence during inventory observations.

Response to Risk

Example Controls to Consider Testing



Control
Construction in progress reviewed for potential impairment
Calculation of capitalized interest is reviewed
Requests for capital expenditure are approved
The system automatically calculates depreciation of assets
Management review for completed projects
Disposals require review and approvals
PP&E activity report is reviewed routinely
Repairs & maintenance expenses are reviewed
PP&E is physically inspected and reconciled to sub-ledger
PP&E classes are reviewed for possible impairment
Manual roll-forward of PP&E is performed and reconciled to the general ledger and source documents

Common Substantive Tests of Details



Test	Assertions
Obtain and reconcile assets movement schedule and detailed listing	C, VA
Test depreciation expense	VA
Test assets additions	E, RO, VA
Test assets disposals	RO, C
Test repairs and maintenance	C
Test impairment of assets	VA

Additional Substantive Tests of Details

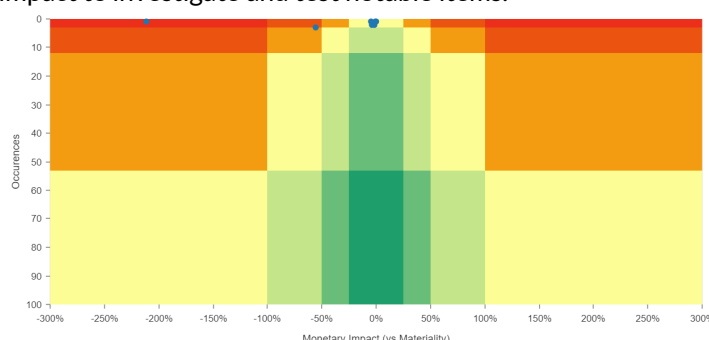


Test	Assertions
Evaluate PP&E accounting policies	ALL
Test utilization of fully depreciated assets	VA
Test useful lives of assets	VA
Test revaluation or fair value of assets	VA
Test assets held for sale	RO, VA
Test capitalization of borrowing costs	VA
Test construction-in-progress movements	E, RO, VA
Test asset grants	VA
Test asset physical existence and condition	E, VA

Audit Data Analytics



Visualize property, plant and equipment transactions by period, user, source document, frequency, and monetary impact to investigate and test notable items.



If you found this helpful, follow me for more



Mark Edmondson

