Evidence, assertions and audit procedures

MODULE 3 | 3.1 | STUDENT COMPANION

Every procedure has one purpose: **sufficient appropriate audit evidence** for the opinion. Sufficiency is quantity; appropriateness is quality, meaning **relevance** and **reliability**. Relevance depends on the **assertion** and on the **direction** of the test. There are **seven types** of procedure, and enquiry alone is rarely enough. When evidence conflicts, the auditor resolves it with more evidence, and a confirmation counts only if the **auditor controls** the whole process.

Sufficient and appropriate

Idea	What it means	In practice
Sufficiency	The quantity of evidence	More is needed where the assessed risk is higher; less where the evidence is of better quality. But no amount of poor evidence makes up for its quality
Relevance	Whether the evidence bears on the assertion being tested	A customer's confirmation shows the receivable exists, not that the customer can pay it
Reliability	Whether the evidence can be trusted	Depends on its source, its nature and how it was obtained, including whether the auditor controlled the process

Information produced by the entity. Reports and listings from the client's own systems must be accurate and complete enough for their purpose before the auditor tests anything with them. Suppose the team plans to use Voltana's monthly report of installations completed to build an expectation of revenue. Before relying on it, the team agrees the report's totals to the system, tests a sample of its lines back to signed completion forms, and checks how the report was generated. A precise test built on an incomplete report gives false comfort.

Relevance depends on the assertion. Attending a stocktake shows that the batteries are there, but not that Voltana owns them; a supplier's invoice and the shipping terms speak to ownership. So the plan is written assertion by assertion, and each procedure is chosen for the assertion it actually supports.

Voltana's evidence plan, assertion by assertion

Revenue

Occurrence

Vouch recorded sales back to signed installation completion forms

Inspection

Cut-off

Test sales either side of 30 June against installation dates

Inspection

Receivables

Existence

Confirm balances with partner electricians

External confirmation

Valuation

Review the ageing and the cash received after year end

Recalculation, inspection

Inventory

Existence

Attend the stocktake and perform test counts

Observation, inspection

Valuation

Compare cost with prices achieved after year end, older models first

Inspection

Warranty provision

Valuation

Build an own range with the engineer; check claims paid after year end and last year's estimate against actual claims

Recalculation, analytical procedures, inspection

Related party lease

Presentation

Check how the lease is described in the statements

Inspection

Disclosures complete and accurate

Agree the note to the lease, the board's approval and the valuation

Inspection

One procedure can be strong for one assertion and say nothing about another

The seven types of audit procedure

1 Inspection

Examining records, documents or a physical asset

e.g. a battery on the warehouse floor

Occurrence and rights; existence of assets

2 Observation

Watching others perform a process or procedure

e.g. staff counting stock

Existence, at that point in time

3 External confirmation

A direct written reply from a third party

e.g. a bank or a customer

Existence; sometimes rights and obligations

4 Recalculation

Checking the arithmetic in documents or records

e.g. recomputing depreciation

Accuracy

5 Reperformance

Independently redoing a procedure or control of the entity

e.g. redoing a bank reconciliation

Accuracy; whether a control worked

6 Analytical procedures

Evaluating plausible relationships between data

e.g. revenue against installations

Reasonableness across a whole population

7 Enquiry

Asking knowledgeable people, inside or outside the entity

e.g. asking about June sales

Used in every audit, but almost never enough alone

Enquiry is everywhere, but never alone. Asking knowledgeable people helps the auditor understand what happened and where to look, and answers given in writing are better than conversations. But an answer is a claim: it needs corroborating evidence from another type of procedure before it supports a conclusion.

Direction decides the assertion

A sale that was never recorded can't be found by examining recorded sales. To test for what is missing, the test must start outside the records.

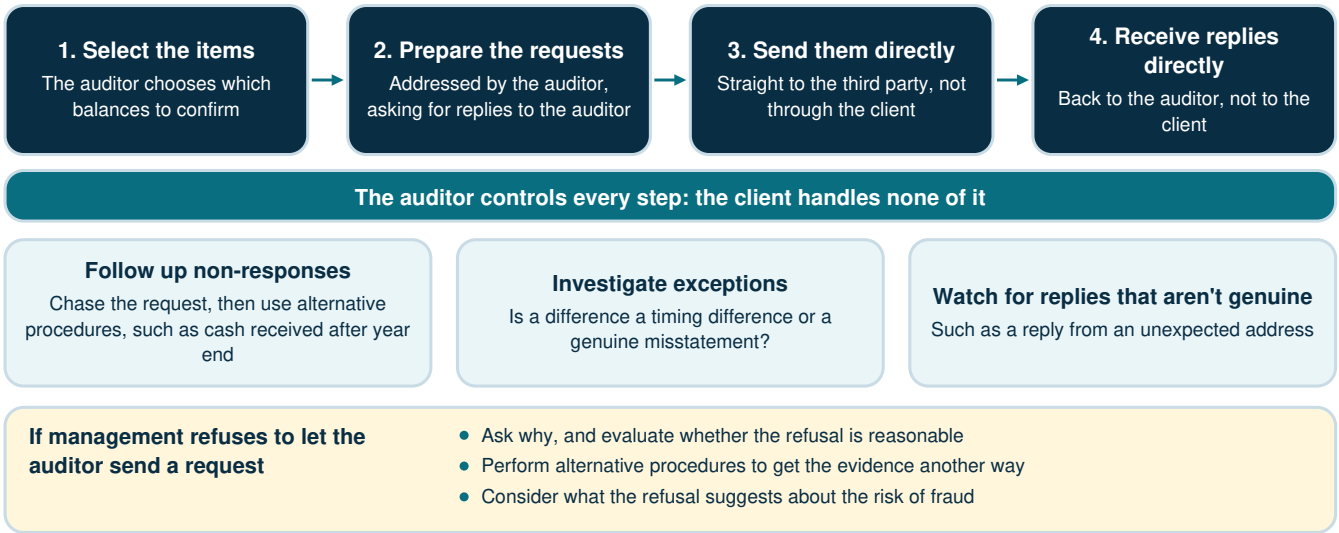
Assertion	Start from	Then look for	Voltana example
Occurrence (and existence)	What is recorded: the sales ledger	Evidence that each item really happened or exists	Vouch recorded June sales back to signed completion forms
Completeness	Independent evidence that something happened	Each item in the records	Trace installations on the installation schedule forward into recorded revenue

When evidence conflicts

Voltana's installation records show a battery installed on 2 July, but the revenue was recorded on 30 June, and the sales manager says the job was really done in June and the record is wrong. The auditor believes neither source yet. When evidence from different sources doesn't agree, or its reliability is in doubt, the auditor works out which further or different procedures will resolve the matter, and considers what it means for the rest of the audit.

- **Ask the customer**, through the auditor, to confirm the installation date.
- **Check the installer's records**, such as phone and route data for that day.
- **Look at the monitoring app**, which shows when the battery first reported data.
- **Think wider:** if the record was right and the sales manager wrong, how many other June sales look the same, and what does that say about the manager's other answers?

A confirmation only counts if the auditor controls it



Why control matters. Once a request or a reply passes through the client's hands, it could have been intercepted, altered or invented, and it stops being independent evidence. Replies that arrive by email, by phone or from an address the auditor didn't use need extra checking, for example by contacting the third party directly using details the auditor has found independently.

Practice questions

MODULE 3 | 3.1 | TRY THESE BEFORE THE WORKED ANSWERS

Question 1 - Match the procedures

Lacewood Bridal Pty Ltd (imagined) runs eight bridal stores. Brides order gowns from the stores' samples and pay a 50% deposit; the balance is paid when the gown is collected after its final fitting. The stores also sell accessories over the counter, charge for alterations, and hold some designers' gowns on consignment. The year ends on 30 June. For each procedure, name the type of procedure and the assertion it best supports.

Procedure	Type of procedure	Assertion it best supports
(a) Watch staff count the veils and accessories at the city store on 30 June		
(b) Ask the main gown designers to confirm directly to the auditor what the chain owed each of them at 30 June, including designers showing nothing owed		
(c) Re-add the listing of customer deposits held at 30 June and agree its total to the general ledger		
(d) Compare each store's monthly gown revenue with the number of gowns collected that month		
(e) Read the consignment agreements with designers whose gowns the stores hold		
(f) Redo a store manager's end-of-day reconciliation of card and cash takings to the sales system		
(g) Ask the head seamstress how alterations are priced and recorded		
(h) Examine the sample gowns in a store for wear and damage		
(i) For gowns collected in the last week of June and the first week of July, compare the date on the signed collection form with the date the revenue was recorded		
(j) Recompute depreciation on the stores' fit-outs		

Question 2 - Occurrence and completeness of Lacewood's sales

Lacewood records each gown order and its deposit in an order system. Revenue from a gown is recognised when the bride collects it and signs a numbered collection form. Accessories are sold through a point-of-sale system, and alterations are charged from numbered job sheets. Design one test of occurrence and one test of completeness for sales, showing where each test starts and which way it runs.

Assertion	Start from (population)	Direction and procedure
Occurrence		
Completeness		

Question 3 - Two pieces of evidence that don't agree

Lacewood's payables ledger shows that it owed Seraphine Atelier (imagined), a gown designer, $18,400 at 30 June. Seraphine's reply to the auditor's confirmation request says $31,600. The difference is one invoice for $13,200, dated 26 June, for six gowns delivered to the city store. Lacewood's accounts manager says those gowns are held on consignment, so nothing is owed until they are sold. How would you resolve the conflict, and what else would you consider?

Worked answers

MODULE 3 | 3.1 | WORKED ANSWERS - ATTEMPT THE QUESTIONS FIRST

Question 1 - Lacewood Bridal

	Type of procedure	Assertion it best supports
(a)	Observation	Existence of inventory, at that point in time (also how well the count is run)
(b)	External confirmation	Completeness of payables (and the obligations owed to designers)
(c)	Recalculation	Accuracy of the customer deposits liability
(d)	Analytical procedures	Occurrence and completeness of gown revenue: the overall reasonableness of the total
(e)	Inspection (of a document)	Rights and obligations: consigned gowns stay out of inventory
(f)	Reperformance	Accuracy and completeness of takings recorded (and whether the reconciliation control works)
(g)	Enquiry	Accuracy of alterations revenue, once corroborated with job sheets
(h)	Inspection (of a physical asset)	Valuation of inventory: worn samples sell at a discount
(i)	Inspection (of documents)	Cut-off of gown revenue
(j)	Recalculation	Accuracy, valuation and allocation of property, plant and equipment

Question 2 - Lacewood's sales (suggested)

Assertion	Start from	Direction and procedure
Occurrence	Sales recorded in the ledger, sampled across the year and weighted to late June	**Vouch backwards** to the signed collection form and the balance received, the alteration job sheet, or the point-of-sale record and card settlement. A recorded gown sale with no signed form may be a deposit wrongly treated as revenue
Completeness	Independent evidence of sales: numbered collection forms and job sheets, each store's daily takings report	**Trace forwards:** check the number sequences for gaps, then follow each form, job sheet and daily total into the sales ledger in the right period. A collected gown with no recorded sale is missing revenue

Question 3 - Seraphine Atelier (sample answer)

- **Find out which source is right.** Does the consignment agreement cover these six gowns? An invoice payable in 30 days suggests a purchase, as consigned goods are usually invoiced only when sold. Check the delivery docket, and whether the gowns were counted as Lacewood's stock.
- **Look after year end.** Paying the $13,200 before any of the gowns was sold points to a purchase.
- **Ask Seraphine again, through the auditor,** about the terms of that delivery. The accounts manager has an interest in the answer, so the explanation alone is not evidence.
- **Decide what it is.** Bought outright: payables are understated by $13,200, and the gowns belong in inventory if they weren't counted. On consignment: leave them out of inventory and payables, and Seraphine's statement is wrong. Then check the other designers' consignment stock and confirmations, and extend the search for unrecorded liabilities.