

Solutions to Student Self Assessment Questions

Chapter 10

Substantive testing, computer-assisted audit techniques and audit programmes

Questions

10.1 Consider the following statements and explain why they may be true or false:

- (a) Tests of controls are those tests designed to check that the accounting and control systems are effective.
- (b) Substantive tests are different in nature from tests of control.
- (c) Audit programmes should be designed to take account of the strengths and weaknesses of the individual entity.
- (d) Audit programmes are developed before the scope decision is made.
- (e) Directional tests are tests of control.

10.2 In this chapter we showed in Figure 10.1 a purchases substantive audit programme, but we did not include the use of audit software. Suggest how audit software could have been used in programme steps 3, 4, 6, 8 and 9. In doing this, state the data on computer file which you would be able to use.

10.3 In Appendix 10.2 on page 392 we suggested steps that could be included in the audit programme for accommodation income of the County Hotel Ltd received in cash. Re-read this appendix and now suggest steps that should be included in the audit programmes for restaurant income received in cash. Explain the reasons for the tests.

10.4 Assuming that your audit programme for the purchase of non-current assets has been completed and that your programme objectives have been met, draft a suitable audit conclusion for audit work carried out in respect of the period from 1 January 2010 to 30 September 2011.

Solutions

10.1 a) *True*

Tests of control are tests directed towards checking the operation of systems. The objective of using them is to prove that the auditor's assessment of control risk is proper.

b) *False*

While the **role** of substantive testing differs from that of tests of control in that it is directed not towards systems but towards proving that transactions and figures are completely and accurately recorded, the **nature** of the tests may be very similar. Thus, selecting goods despatch notes to prove that the entry to inventory records is accurate may be used to both to test the operation of the inventory and purchases systems AND in substantive testing to prove that inventory records and purchases are complete and accurate.

c) *True*

Audit programmes should be tailor-made to the circumstances of the particular organisation. For instance, if the auditor discovered that credit control procedures were weak, the audit programme should emphasise steps to prove collectability of the recorded trade receivables.

d) *False*

Audit programmes give effect to the scope decision and therefore must be drawn up after the scope decision has been made.

e) *False*

The purpose of directional tests are to test for over- and under- statement of transactions or figures or balances and such tests should therefore be regarded as substantive tests of details.

10.2 Audit software could have been used in the following manner. We have assumed that the software contains a random number generator.

Programme step 3:

- a) The sequence of purchase orders could be checked by computer software that could also make a random selection of these orders. It could marry the selected purchase orders with the related goods received note.
- b) The software could make a random selection of receipts in the inventory records and compare with goods received notes.

Programme step 4:

The software could check the sequence of goods received notes.

Programme step 6:

The software could select the goods received notes randomly and compare with purchase order, inventory records and recorded purchase invoices, assuming that the record of invoices contain quantity data.

Programme step 8:

The purchase invoices could be compared with entries in the purchase day book and purchase (creditors) ledger.

Programme step 9:

Trade payables' balances could be selected randomly.

10.3 Major matters to be considered for inclusion in audit programmes for restaurant income of The County Hotel Limited received in cash include the following:

Much of this income, particularly that relating to non-residents, is likely to be in cash, but some will be on credit. It is likely that residents will ask for meals to be added to their bill. A particular problem for the auditor is the large number of different meals available in the restaurant in circumstances of poor portion control. Portion control is the procedure to control the amounts placed on each plate and the related costs. Auditors should establish the 'normal' relationship between restaurant costs and income. Clearly, if portion control is poor it will be difficult to control restaurant costs and there may be no constant relationship between costs and revenue. This problem may be greater if temporary staff are employed, as is often the case in restaurants. The auditor's interest is to ensure that restaurant income is accurately and completely recorded.

Programme step: Refer to restaurant costs and income work programme and confirm that our work has enabled us to conclude that such income is fully and accurately recorded. The audit programme in the restaurant income section should include the following steps:

- a) Review restaurant income for the year to date and the corresponding period last year and enquire into any significant changes in total income and table usage. The actual and potential effect of the new chef should be discussed with management.
- b) Using management information and statistics, discuss with management the reasons for any changes. In particular, the effect of any policy change by management on table usage should be noted. Enquiries into the correlation between restaurant

- income and accommodation income should be made in conjunction with the accommodation income work.
- c) Review management estimates, showing that restaurant capacity break-even point is 55%.
 - d) In view of poor portion control, discuss with the head cook and headwaiter (independently of each other), the average quantities of food used per plate for popular selected dishes. (But note that portion control is now said to be more effective than in the past).
 - e) Check the numbered menu in the restaurant (for breakfast, luncheon and dinner) to the computer master file, ensuring in particular that standard prices are accurate.
 - f) Check: that:
 - i) Waiters' pad copies agree with cash desk and accounts copies and have all resulted in the preparation of invoices
 - ii) The total of the invoices issued for cash on selected days equal the amount recorded in the restaurant cash till and cash book.
 - iii) All entries, including price, on the waiters' pads agree with the master file menu details.
 - iv) Waiter's pad copies agree with kitchen copies
 - g) Check that kitchen costs as recorded appear reasonable in relation to restaurant income.
 - h) Perform purchases depth test on food orders, deliveries, invoices (matching operation) and subsequent recording in purchases record.

10.4 Suggested audit conclusion on the purchase of fixed assets

On the basis of the work performed on the purchase of fixed assets as set out in the fixed assets audit programme on working paper **F100**, as supported by working papers **F101** to **F105**, I can conclude that, within reasonable limits, all purchases of fixed assets in the period from 1 January 2011 to 30 September 2011 have been fully and accurately recorded and that such purchases have been made on the basis of properly prepared budgets duly authorised at appropriate levels within the company. The audit programme was prepared on the basis of scope decisions recorded in working paper **F10**, supported by systems notes in the permanent audit files (Section **F**).