Audit Evidence
Prove It to Me!

Dallas II A –CAST
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Presented by:

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Objectives

- Familiarity with the IIA Standards on Audit Evidence.
- Practical examples of gathering audit evidence.
- Best practices in conducting audit fieldwork.
evidence (ev-i-duhns)
1. that which tends to prove or disprove something; ground for belief; proof.
2. something that makes plain or clear; an indication or sign
3. Law. data presented to a court or jury in proof of the facts in issue and which may include the testimony of witnesses, records, documents, or objects.

Dictionary.com
Evidence in its broadest sense includes everything that is used to determine or demonstrate the truth of an assertion.

Wikipedia.com
2300 – Performing the Engagement

Internal auditors must identify, analyze, evaluate, and document sufficient information to achieve the engagement’s objectives.

2310 – Identifying Information

Internal auditors must identify sufficient, reliable, relevant, and useful information to achieve the engagement’s objectives.
2320 – Analysis and Evaluation

*Internal auditors must base conclusions and engagement results on appropriate analyses and evaluations.*

2330- Documenting Information

*Internal Auditors must document relevant information to support the conclusions and engagement results.*
the audit office

video intro
THE ASSURANCE ENGAGEMENT PROCESS

Plan
- Determine engagement objectives and scope.
- Understand the auditee, including auditee objectives.
- Identify and assess risks.
- Identify key control activities.
- Evaluate adequacy of control design.
- Create a test plan.
- Develop a work program.
- Allocate resources to the engagement.

Perform
- Conduct tests to gather evidence.
- Evaluate evidence gathered and reach conclusions.
- Develop observations and formulate recommendations.

Communicate
- Perform observation evaluation and escalation process.
- Conduct interim and preliminary engagement communications.
- Develop final engagement communications.
- Distribute formal and informal final communications.
- Perform monitoring and follow-up procedures.
Performing the Engagement

1. Conduct tests to gather evidence
2. Evaluate evidence gathered and reach conclusions
3. Develop observations and formulate recommendations
the audit office

performing the audit engagement
### ILLUSTRATIVE APPLICATIONS OF MANUAL AUDIT PROCEDURES

<table>
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<tr>
<th>Procedures</th>
<th>Illustrative Applications</th>
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| Inquiry      | • Circulate a questionnaire among senior executives asking them to identify the “top 10” risks threatening the organization.  
• Ask the organization's outside legal counsel to provide information about any litigation, claims, and/or assessments against the organization.  
• Interview managers and employees involved in the cash disbursements process to identify key process control activities. |
| Observation  | • Tour the auditee's facility to gain a general understanding of day-to-day operations.  
• Observe the care with which employees count the year-end physical inventory.  
• Watch employees involved in executing and recording cash disbursements transactions to determine whether they are performing their assigned responsibilities and only their assigned responsibilities. |
| Inspection   | • Review the minutes of board of director's meetings looking for authorization of significant events, for example, the acquisition of another company.  
• Inspect selected inventory items to determine their condition and salability.  
• Read the cash disbursements policies and procedures to obtain an understanding of key elements of the process, for example, assigned roles and responsibilities. |
| Vouching     | • Vouch a sample of inventory items from the accounting records to the warehouse to see that the inventory items exist.  
• Vouch a sample of sales invoices to corresponding shipping documents to verify that the shipments occurred.  
• Vouch a sample of check copies to supporting voucher packages to test the validity of the checks. |
| Tracing      | • Trace internal auditor test counts of inventory to the auditee's inventory compilation records to verify that the counts are properly included in the compilation.  
• Trace receiving reports for goods received to the corresponding voucher and then to the voucher register to verify that the receipts of goods are properly recorded as liabilities.  
• Trace checks dated within a period of several days before and after year-end to the accounting records to ensure the checks were recorded in the proper year. |
| Reperformance| • Recalculate accumulated depreciation and depreciation expense to verify that they were calculated correctly.  
• Independently estimate the allowance for doubtful accounts to test the reasonableness of the accounting department's estimate.  
• Reperform auditee-prepared bank reconciliations to test whether they were completed correctly. |
| Analytical procedures | • Prepare common-size financial statements for the current year and preceding two years; look specifically for variance or unexpected trends.  
• Compare the organization's common-size financial statements with published industry common-size information looking for unexpected inconsistencies.  
• Calculate accounts payable turnover for the current year and preceding two years as evidence of vendor payment periods. |
| Confirmation | • Confirm a sample of accounts receivable subsidiary ledger balances with customers.  
• Confirm the principal balance of a notes payable and interest rate with the lender.  
• Confirm cash account bank balances with banks. |
KEY COMPONENTS OF EFFECTIVE INTERVIEWING

Interviewing objectives:
- Gather information (that is, audit evidence) relevant to the engagement.
- Establish a rapport that fosters a positive working relationship throughout the engagement.

The interviewing process:
Preparation for the interview:
- Define the purpose.
- Identify the appropriate interviewee.
- Gather background information about the audit area and interviewee.
- Create the right set of questions (what, why, how, where, when, who).
- Establish expectations with the interviewee and identify information needs.
- Arrange logistics (date, time, location, length).
- Prepare an outline.

Conduct the interview:
- Establish rapport and create an atmosphere that encourages openness.
- Review the purpose of the interview, the topics to be covered, and the estimated time needed.
- Ask straightforward questions and meaningful follow-up questions.
- Avoid technical jargon.
- Use periods of silence effectively.
- Listen.
- Summarize and confirm key points.
- Discuss next steps.
- Arrange follow-up contact.
- Thank the interviewee.

Document the interview outcomes (as soon as possible after the interview):
- Reflect on the interview and review notes.
- Record the results of the interview in good form.

Characteristics of effective interviewers:
- Professionalism (for example, being prepared, respectful, courteous, and on time).
- Outstanding interpersonal and oral communication skills, including listening skills.
- The capacity to display confidence and command respect without being arrogant.
- An innate curiosity.
- Objectivity (that is, remaining impartial and refraining from interjecting personal opinions).

Common barriers to effective interviews:
- Audittee impediments such as competing demands on time, preconceived notions about internal auditors, and fear of reprisal.
- Flaws in the interview process.
- Lack of requisite competencies on the part of the internal auditor.

Critical success factors:
- Be prepared.
- Know and respect the interviewee.
- Establish credibility and trust.
- Speak the interviewee’s language.
- Expect the unexpected.
2. Evaluate evidence gathered and reach conclusions

1) **SUFFICIENT** (Quantity)
   - Factual
   - Adequate
   - Convincing
   - Prudent person would reach a similar conclusion

2) **COMPETENT** (Quality)
   - Reliable
   - Best Attainable

3) **RELEVANT**
   - Supports Audit Findings and Recommendations
   - Consistent with Audit Objectives

4) **USEFUL** (Helps organization meet its goals)
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<tr>
<th>Levels of Reliability</th>
<th>Descriptions</th>
<th>Example Documents</th>
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| High                  | Documents prepared by the internal auditor  
Documents sent directly from a third party to the internal auditor | Inventory test counts  
Process maps  
Risk and control matrices  
Confirmations  
Cutoff bank statements  
Letter from outside attorney |
| Medium                | Documents created by a third party, sent to the organization, and requested from the organization by the internal auditor  
Documents created by the organization, sent to a third party, returned to the organization, and requested from the organization by the internal auditor | Vendor invoices  
Customer purchase orders  
Bank statements  
Remittance advices  
Canceled checks  
Deposit slips |
| Low                   | Documents created by the organization and requested from the organization by the internal auditor | Written policy statements  
Receiving reports  
Time cards |
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the results
CAE Best Practices and Recommendations

- Make sure you come to the correct conclusions. For example, a missing conflict of interest form could really be an indicator of a conflict of interest issue rather than noncompliance with a policy.
- State **WHY** you have reached a conclusion.
- Don’t assume...or.....
- Tie controls to audit test work.
- Evidence must support the findings.
- Think outside the box.
- Don’t work in a silo.
CAE Best Practices and Recommendations

- Does the evaluation of the evidence support the observation and/or the working paper conclusion? (does the auditor conclude that supporting documentation is sufficient when there is an error rate of 10/30 items that lack documentation?)
- Quality of the audit evidence. (are the invoices originals?)
- Does the audit evidence link electronically to a web document that may not exist in the future?
- Knowing **when** to use various types of audit evidence.
- Knowing **how much** and what evidence to put in the working papers.
CAE Best Practices and Recommendations

- “Use your brain.” Think think think.
- Question deviations, exceptions or irregularities in the audit evidence.
- If someone tells you they perform a control process and it's not documented, write down your understanding and have that person attest to it.
- The organization of the evidence should be done in a manner that logically makes sense and clearly shows how the auditor came to the conclusion he/she did.
- Use a camera! Video surveillance cameras?
- Document your sources, including titles.
CAE Best Practices and Recommendations

- Document in a **timely manner** before you forget what you did!
- When sampling – provide adequate evidence for your sample selection (population, type sample, audit software parameters, etc.)
- Request documentation to support management assertions.
- **Question** what you are given.
- Answer the questions: **who, what, when, where, how, why?**
- For audit findings, focuses on the root causes of the problem(s) – staff should try to get at the root causes of problems and not just report errors.
- But…avoid rabbit trails!
Do you want a prize?
Which of the substantive fieldwork procedures presented below provides the best evidence about the completeness of recorded revenues?

a. Reconciling the sales journal to the general ledger control account.

b. Vouching charges made to the accounts receivable subsidiary ledger to supporting shipping records.

c. Vouching the shipping records to the customer order file.

d. Reconciling shipping records to recorded sales.
One of the audit objectives for a manufacturing company is to verify that all rework is reviewed by the production engineer. Which of the following audit procedures would provide the best evidence for meeting this objective?

a. Trace a sample of entries in the rework log to remedial action taken.
b. Trace a sample of rework orders to entries in the rework log.
c. Trace a sample of entries in the review log to rework orders.
d. Trace a sample of rework orders to entries in the review log.
The auditor must determine the applicable laws and regulations. Which of the following procedures would be the least effective in learning about the applicable laws and regulations.

a. Make inquiries of the city’s chief financial officer, legal counsel, or grant administrators.
b. Review prior year working papers and inquire of officials as to changes.
c. Review the applicable grant agreements.
d. Discuss the matter with the audit committee and make inquiries as to the nature of the requirements and the audit committee’s objectives for the audit.
Ordinarily, what source of evidence should most affect audit conclusions?

a. External.
b. Inquiry.
c. Oral.
d. Informal.
What standard of evidence is satisfied by an original signed document?

a. Sufficiency
b. Competence
c. Relevance
d. Usefulness
In Summary... the Key to Audit Evidence
For More Information...
Starring:
• Michael Callahan as Tony Messermasick
• Michael Callahan as “Larry”
• Michael Callahan as “hot dog eating contest cheerleader”
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• Chris Hes as John Taylor
• Adrienne Adame as Lynn Johnson
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