

### ***Week 3 - DQ 1***

***What are the two types of audit tests? What are some examples of each of these two types of tests? How will the auditor use the data gathered from these tests?***

#### ***Response #1***

The two types of audit tests are tests of control and substantive tests. According to Boynton and Johnson (2006), a test of controls is employed "to determine effectiveness of design and operation of internal controls", whereas a substantive test is employed "to determine fairness of significant financial statement assertions". An example of tests of control would be inspecting original records such as checks, journal entries, invoices, memos, receipts, and vouchers that support and/or serve as proof of a business transaction. Another example, would be inquiring of client personnel, and observing client personnel performing controls. A substantive test example would be using analytical procedures, such as ratios and percentages to decide the accuracy of the tests of control. According to the AICPA the auditor "should use the information gathered by performing the risk assessment procedures to evaluate the design of controls and determining whether they have been implemented as audit evidence to support the risk assessment". In other words, the data should be used to the test the effectiveness of the design and operation of the related necessary control. On the other hand, an auditor should use the data gathered from the substantive test to determine if a financial statement account is fairly stated, and to either ensure accuracy or to identify risks of misstatement.

#### ***Response #2***

Two types of audit tests are tests of controls and substantive tests. Tests of controls are procedure of the effectiveness of the implementation and design of internal controls. The auditor evaluates the control of the design to determine that the control has been properly designed to prevent material misstatements. Examples of tests of controls include inspection of electronic files, documents and reports. Substantive tests provide evidence of management's fair presentation of assertions in financial statements. Some substantive

tests include tests of details of transactions and balances. For example, tests of details of transactions include examination of documents such as a bill of lading or a recorded invoice. A test of balances is the examination of the general ledger. For example an auditor could obtain evidence by sending a customer a confirmation that they owe a receivable. The auditor will use the data gathered from these tests to identify audit issues. The tests will compare the auditor's expectations with the recorded values and will help the auditor understand the business being audited to identify the high risk areas. The data gathered from these tests allow an auditor to achieve detection risk and determine if the audit risk is reduced to a manageable low level.

### *Response #3*

Two types of audit tests are the substantive test and the test of controls. The substantive tests are used to detect errors in an account balance or disclosure element in financial statements. Substantive tests are concerned with monetary misstatements and can be classified as tests of details of transactions and account balances, which seek to identify errors in individual transactions and account balances by bank confirmation, walk through tests, etc., and substantive analytical tests, which compare auditor's expectations to recorded data. Some substantive analytical tests include trend analysis, ratio analysis, or reasonableness analysis. The test of controls refers to procedures which measure the operating effectiveness and efficiency of controls in order to detect and prevent misstatements. Test of controls are necessary when the substantive procedures do not provide sufficient audit evidence. Some examples of the test of controls include the inspection of reports and documents as well as certain inquiries of staff members and senior management. The auditor will use data gathered from these tests to develop an expectation, compare the expectation to the recorded amount, then direct attention to higher risk areas where they can conduct focused tests of details.

#### *Response #4*

The two types of audit tests include a performance of test controls and substantive test approach. The audit test for test controls “should provide evidence about the effectiveness of the design and operation of the related necessary control” (Boynton & Johnson, 2006, p. 475). The auditor carefully analyzes the test evidence and the cost of the test in its analysis. An example of a performance test of controls is when I use the accounting program at my job. The auditor would compare the amount of money used in cash disbursements and checks cut and would evaluate whether or not it is an effective for the recording of those transactions. The auditor will use the data gathered from this test to ensure that the internal controls of a business are working effectively.

The substantive test approach is used to determine the financial statements significance and fairness of the assertions. Examples of the substantive test include an evaluation of the initial business's procedures, the analytical procedures, and performing a test of the details in the company's transactions. The substantive test also is required by the GAAS. The auditor will use the data gathered from this test to ensure the financial statements are completed correctly, provide accurate information and that all information correlates with the financial statements.

#### ***Reference:***

Boynton, W. C., & Johnson, R. N. (2006). *Modern auditing: Assurance services and the integrity of financial reporting* (8th ed.). Hoboken, NJ: John Wiley & Sons.