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Audit working papers

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achieve complete success when it comes to the writing of comments. He must first know what it is about which he wishes to write. He must next set down his thoughts in such manner that there will be no doubt in the mind of any subsequent reader, be he client or a presumably disinterested person; be it the following day or twenty-five years later.

In order that in an organization of any size where a number of persons prepare reports, such reports shall be uniform, some form of review of the reports in the rough is necessary. It is perhaps this feature of his work that the accountant-in-charge finds most difficult. Having given the report the best of which he is capable, he is inclined to be hurt at what he regards

as the mutilation of his work. A moment's pause for reflection will frequently help this feeling. When he considers that this has the purpose of affording him highly specialized assistance in the preparation of his report, as well as making for uniformity, he will perhaps view the proceedings with more equanimity.

The characteristics of a good in-charge accountant are vision, ability to plan and organize, energy, capacity, good address, assimilativeness, elasticity, decisiveness. In addition he must be a good mixer, a person of character and refinement, and a good essayist. With these qualifications he is sure of occupying an important place in a profession which is already coming into its own.

Audit Working Papers

(A paper read by Mr. W. H. Bell before the Tri-State Society of Certified Public Accountants, at Baltimore, Maryland, June 24, 1919.)

THE importance of the substance and form of working papers is threefold: first, to the accountant originating the papers, not only in the audit procedure and the preparation of his report, but in answering questions that may later arise from any source; second, to the person or persons who review and check the report; and third, to the accountant making a subsequent audit.

There are two general tendencies regarding the data contained in working papers, viz., deficiency and superfluity. It is probable that the latter is more prevalent than the former, but that the tendency to prepare superfluous working papers diminishes in direct ratio to an accountant's advance in proficiency as an auditor, that is, as he becomes more practical. Granting that an accountant charged with the preparation of working papers has the requisite knowledge of the principles of auditing, it should be almost unnecessary to tell him what to do, except as a means of facilitating his

work, other than by telling him what not to do.

The most glaring examples of superfluous work, or misdirected energy, are mere transcripts of accounts, or so-called analyses of accounts designed to classify the entries, which utterly fail to accomplish what might be written on one line. The principles actuating accountants in preparing such papers appear to be to obtain information, no matter how unreliable or unnecessary, and to check the mathematical accuracy of the accounts in that manner. Practically, they are often meaningless figures. Cases in point are: analyses of reserves for depreciation without determination of the rates and the asset values constituting the bases for the credits and without information regarding the charges; elaborate tabulations of sales, cash receipts and disbursements, accounts receivable and payable controlling accounts, etc., the only practical benefit from which may usually be derived in a great deal less time by

checking the footings and a few postings on the books; schedules of accounts receivable, unpaid vouchers, etc., prepared by the accountant, when the client's trial balances may usually be utilized to equal advantage.

On the other hand, it is well to recognize the aid to the memory in recording what is brought to the attention; also the fact that the act of writing may serve to impress upon the mind what might otherwise be overlooked. As an example of the application of the latter principle may be cited summaries of inventories. It is well known that the verification of computations of inventories becomes somewhat monotonous, and that therefore important factors may be overlooked if the accountant's attention is not abruptly arrested by means of writing a summary. Recently it was found that an assistant accountant overlooked erroneous additions and deductions in the summary of an inventory which were of considerable importance. There is little doubt that the facts would have been forced upon his attention by writing the items; if not, they would certainly have been disclosed to the accountant in charge of the work.

It may seem rudimentary, but is nevertheless important, that every letter and figure in working papers should be legible to others as well as to the accountant himself. In searching through papers for information elucidating some assertion in a report, reviewers have even found memoranda in shorthand, which might as well be in Sanskrit for their use. This precaution regarding legibility applies particularly to names. If these are to be used in a report they should be typewritten if practicable; if not, they should be printed or written with great care. Abbreviations should not be used when there is any possibility of their being misunderstood.

We do not favor the use of ink in preparing working papers, believing that there are too many occasions for erasures and that there is no practical advantage to offset the additional time required.

It is extremely important that each paper bear the initials or, preferably, the full name of the person responsible therefor.

It is desirable that papers be of standard size, so that the larger sheets of analysis paper, when folded, will be uniform in size with the journal or memorandum paper. The principal advantage of this is that it is conducive to a more orderly condition of the files, but it also tends to obviate loss or misplacement. It would be ideal if all memoranda were made on sheets of standard size, but perhaps it is of greater importance that all papers be preserved that can even remotely be regarded as having a future value. It is said that a law suit has been won through the preservation by an accountant of a piece of scratch paper showing a multiplication. However, odd pieces of paper may be pasted or securely attached to standard size sheets, thus affording greater assurance of their being preserved.

It is important that only one side of the paper be used. Writing on the back of a sheet may easily be overlooked. Paper is cheap, even at present prices, as compared with the impairment of efficiency resulting from too great economy.

Each sheet should be headed with a terse description of what it purports to be, including the name of the engagement and, usually, the date or the period covered by the audit, to avoid possible confusion with other papers. When sheets are folded the same information should appear on the outside.

While it is largely a matter of individual preference as to whether all papers shall be fastened together, we fail to see any advantage in it, excepting as to irregular size sheets, and believe that a judicious use of folders is better, especially considering the additional work of cutting or folding the larger sheets for the purpose of attaching them, and the greater facility of reference if they are loose.

During the early stages of the work the

accountant should acquaint himself with the accounting system in use and the office personnel. Unless the client's organization is comparatively small, it is usually desirable to include in the working papers a list of the books and records that will be used in the audit, the names of the persons keeping such records, and of officers, etc., with whom the accountant or his assistants will come in contact, and such information as the names of persons authorized to approve vouchers, sign checks, etc. This memorandum can also be utilized in conducting future audits.

When the accountant has progressed far enough in the work to formulate a comprehensive plan, he should prepare a work sheet or audit program. One such program may be made to cover several periodical audits if good judgment be exercised in giving effect to changing conditions. For this purpose a columnar sheet may be used, with the various details of work to be done listed down the left side and the columns headed, in pairs, with the dates of the respective periods to be covered. One of each pair may then be used for the initials of the person doing the work and the other for the date on which performed. When certain parts of the audit are limited to tests, such as the verification of vouchers, footings, sales invoices, postings, etc., the work sheet should show what periods, or what approximate percentage of accounts, etc., were selected and examined. The word "test" is subject to much abuse unless properly safe-guarded. It is often advantageous, also, to make a note on the work sheet of the time devoted to certain phases of the work. It is generally inadvisable to use the same work sheet for two periods as far apart as a year. However, it is desirable for an accountant to familiarize himself with the work of the previous year, as a basis for his judgment regarding the work to be done, by reviewing all of the working papers used at that time.

(To be continued)

Meetings.

THE practice of having a meeting of members, managers, and heads of departments was inaugurated at the Executive Offices, Tuesday, June 17, 1919. It is planned to hold these meetings every other Tuesday at two o'clock in the afternoon, and to have them extend over a period of about one hour. At such times there will be discussed matters pertaining to our organization and work. It is hoped that members and managers from out of town will, by their presence, add to the pleasure and value of the meetings when their visits to New York coincide with the days on which meetings will be held.

The following announcement, which will, we think, be of interest to everyone in the organization, is quoted in part from General Order No. 69 of the War Department, under date of May 24, 1919:

"Awards of distinguished-service medal.—By direction of the President, under the provisions of the Act of Congress approved July 9, 1918 (Bul. No. 43, W. D., 1918) the distinguished-service medal is awarded to the following-named officers and civilians:

* * * * *

Colonel Arthur H. Carter, Field Artillery, United States Army (discharged). For exceptionally meritorious and conspicuous service. While on duty in the office of the Chief of Field Artillery, he displayed great ability in developing the organization of the Field Artillery Central Officers' Training School; he then proceeded to Camp Taylor, established this school and administered it in an exceptionally meritorious manner during the remainder of the war.

* * * * *

By order of the Secretary of War,
PEYTON C. MARCH,
General, Chief of Staff.

Official.
P. C. HARRIS,
The Adjutant General."

degree of Doctor of Divinity was substituted. Where it was desired to confer more than the usual honor, the double LL.D. was used.

The fields of commerce, accounts, and finance received academic recognition in 1900, when, through the efforts of a group of accountants in New York City, among whom the late Charles Waldo Haskins was prominent, New York University established the first school of commerce, accounts and finance in the country.

This school and the many others which have followed have done much to revise academic traditions. In the same way recognition of these fields of endeavor and the men engaged therein has quickened the thought of those involved to the propriety, when honoring men in these fields, of conferring upon them degrees with more significance than that of Doctor of Legal Law. For this purpose the degree of Doctor of Commercial Science was evolved.

Union College granted the first degree of this kind to Dean Joseph French Johnson of New York University School of Commerce, Accounts and Finance in 1909. New York University granted the degree for the first time in June, 1916, and has since conferred it annually. It has honored men who, by reason of their achievements in their respective fields have fully merited the honors. The list consists of Jacob Henry Schiff and Elijah Watt Sells in 1916; Theodore Newton Vail and Paul

Moritz Warburg in 1917; Charles Michael Schwab in 1918; Thomas Coleman du Pont and Henry Robinson Towne in 1919.

Vice Chancellor Stevenson of New York University presented Mr. Sells for the degree of Doctor of Commercial Science to the Acting Chancellor, Rev. George Alexander, on June 8, 1916. Dr. Alexander conferred the distinction with the following words:

“Elijah Watt Sells, for pre-eminence in a department of human effort in which the prime essentials are accuracy and truth, for the prevision which prompted you to secure for accountancy academic recognition, for distinguished service rendered to local governments, and especially to the Government of the United States, both at home and abroad, I confer upon you, by the authority of New York University, the degree of Doctor of Commercial Science.”

Baker University previously conferred the honorary degree of Master of Arts upon Mr. Sells in 1909.

There is little in the way of worldly gifts to reward such men as have received the honorary degree of Doctor of Commercial Science. It is well that there is left something which vain-glorious striving will not secure. To be honored by this, the choicest gift which mankind has to offer, must indeed bring a thrill of satisfaction and pleasure.

Audit Working Papers (Concluded)

(A paper read by Mr. W. H. Bell before the Tri-State Society of Certified Public Accountants, at Baltimore, Maryland, June 24, 1919.)

The basic working paper, the backbone of the working papers, is the general ledger trial balance. Virtually all other papers relate to the items shown on the trial balance. It is usually desirable for the accountant to draw off a trial balance himself. It should always be included in the working papers in any event, that is, the

client's trial balance book should not be checked and the statements prepared therefrom; and it will be found that time is seldom saved by utilizing the client's printed or typewritten form. These comments on the general ledger trial balance are intended to include the trial balance of a private ledger, if any; if there be more

than one ledger containing general or financial accounts the trial balances should be combined, either by eliminating the controlling accounts for the purpose, or otherwise. Of course there may be exceptional cases where the private ledger accounts are of such a confidential character that the trial balance of that ledger should not be exposed by being used in conjunction with that of the general ledger. In such cases the former should be treated as an analysis or schedule of the latter.

It is usually desirable to treat the profit & loss accounts, whether before or after closing, as a part of the general trial balance. This will necessarily be done if the closing entries have not been made, and it is believed that the procedure is advantageously simplified, in the great majority of audits, by having only one series of supporting analyses and schedules. If subsidiary operating ledgers be kept it is usually advisable to treat the trial balances thereof as analyses supporting the general ledger trial balance.

There are few trial balances so small but that it is desirable to separate the debits from the credits, putting the latter on a separate sheet or on the bottom of the same sheet. Where there are few accounts, and especially if the books have not been closed, it is usually satisfactory to make no distinction at first between classes of accounts and to arrange the trial balance in columns as follows, with separate sheets or sections for the debits and credits:

Ledger Folio

Name of account

Balance at beginning of period

Balance at end of period, per books

Adjustments, in one or two columns
—increases in black and decreases in red, both in one column, or debits in one column and credits in the other

Balance as adjusted, in two columns
—one for assets or liabilities and the other for profit & loss charges or credits

Remarks

Reference to supporting papers.

In perhaps the majority of cases, however, it is considered desirable to show separately the asset and liability and the profit & loss debit and credit accounts, that is, on four sheets or parts of sheets. Then only one column is required for the final figures. If the books have been closed it is usually desirable to place the liability accounts immediately after the asset accounts, and effect a balance. Then should follow the debit and credit profit & loss accounts, which should also be made to balance by including in the credits the balance at the beginning of the period, and in the debits the balance at the end—assuming, of course, that they are both credit balances. If the books have not been closed it is usually not worth while to thus balance both the balance sheet and the profit & loss accounts, but the preparation of the statements is facilitated by doing so eventually.

In the case of monthly, or perhaps quarterly, audits, one trial balance may be used for a number of periods, as it is usually unnecessary to provide columns for adjustments, etc. It will be found advantageous in such trial balances to work from right to left, that is, to have the latest figures nearest the name of the account.

When the classification of items in the balance sheet and the profit & loss statement, and the number of accounts on the trial balance, can be foreseen with reasonable accuracy, as would be the case if the accounts have been audited before, it is often an advantage, especially on a voluminous trial balance, to group the items as they will be recapitulated in the statements, without regard to their sequence in the ledger. This will usually obviate the preparation of special grouping sheets.

To summarize, the arrangement of the trial balance should be varied, if necessary, to suit the particular conditions, as, more than any other factor, it will facilitate or impede the work of all who, for any purpose,

have occasion to use the working papers.

All adjustments made by the accountant during the progress of the audit should be prepared in his papers in journal entry form, with the same care regarding explanations that he would exercise if he were making the entries on the books. All entries should be numbered, and a separation made between those made on the books, if any, and those necessary to reconcile the balances of the accounts as shown by the books and as adjusted by him. If the trial balance has been originally taken off before closing, and there are many adjusting entries in closing, it may be desirable to take off another trial balance, on the same sheet, after closing, rather than make all of these entries in his papers. At any rate, the final trial balance taken off the books should be the basis for all figures subsequently used, and any adjustments thereof should be shown in the papers. The adjusting entries, with their numbers, should be posted to the trial balance in the column or columns provided for the purpose. If, however, there are many entries affecting one account they may be recapitulated and posted as one item. The adjustment column or columns of the trial balance should be footed to see that they balance. All adjustments should be applied to supporting analyses or schedules as well as to the trial balance.

In the space provided on the trial balance for remarks should be noted any information regarding the nature of, changes in, or verification of the accounts when it has not been considered necessary to prepare supporting papers. There are very few items on a trial balance, other than those requiring analysis or supporting schedule, that do not call for some comment, if only "no change," which remark may be ample in the case of property accounts if there has actually been no change; this should not be inferred from the fact that the balance at the end of the period is the same as at the beginning.

In the last column of the trial balance

should be shown the reference number of papers relating to the account. All analyses or schedules of accounts, or other data relating thereto which cannot be indicated on the trial balance itself, should be numbered conspicuously, preferably in colored pencil, and the number should be shown on the trial balance. If appropriate, the same sheet may be used for more than one account, but unless there would be unnecessary repetition or waste of paper, it is better to use separate sheets. Supporting papers are usually numbered in the order of the appearance of the items on the trial balance, but this is by no means essential; in fact it is usually desirable to put the bulkier papers at the back of the folder. All supporting papers pertaining to one account should be fastened together and similarly numbered. This applies to confirmations, unless their bulk precludes attaching them to the other papers, in which case their location should be definitely shown by some method of indexing. If a confirmation cover more than one subject—for example a bank's certification of cash balance, notes payable, and securities held as collateral—and it be attached to the cash papers, reference should be made thereto opposite the related items on the analyses of notes payable and securities pledged. It is often desirable to distinguish between sub-analyses by a series of letters, which should be indicated plainly on the main analysis.

Any papers which do not relate directly to a trial balance item should be placed in a special folder and, if there be many, should be indexed on the cover. Among such papers will be the work sheet or audit program, memorandum regarding salient features of the accounting system, etc., excerpts from by-laws and minutes, various agreements, data regarding contingent assets and liabilities not on the books, copies of the client's statements, and memoranda prepared during the progress of the audit relating to points to be covered in the report.

The accountant should be so methodical in the preparation of the statements for his report that each item can be readily traced back to the trial balance. Unless the accounts in the trial balance are so few that they are carried as such to the statements, or the trial balance has been specially arranged to show the constituent items of the statements, as explained in the foregoing, it will be necessary to prepare grouping or assembly sheets for the purpose. These usually contain simply the captions used in the statements and the component trial balance items. If the classification be elaborate, and the accounts numerous, it is usually well to designate the captions by letter or number, referring thereto on the trial balance. In rare cases it will be found convenient to apply adjustments to the grouping sheet instead of to the trial balance.

Perhaps it is not especially germane to this subject, but attention is directed to the necessity for being certain that the figures used in the preparation of statements, through the grouping sheet or trial balance, "tie up" to the supporting analyses and schedules; also that the profit & loss balance used in the balance sheet is the same as that shown in the profit & loss statement. It is well to use a distinctive check mark to indicate final approval of the trial balance items. In this connection, care should be exercised in making last-minute changes, to see that a clear record is left in all the working papers affected.

With regard to the various analyses, etc., almost all that can be said in such a general discussion as this is that, both as to content and form, they should be adapted by the accountant to meet the exigencies of the situation which he faces. Attention has already been directed to the folly of making mere transcripts of accounts when it is the intention to check their accuracy or bring out certain of their salient features. Further, analyses may often be combined to good advantage; for example,

additional columns on the analyses of notes receivable, notes payable, and investment securities will take the place of separate analyses of interest accrued or paid in advance, profits and losses on sales of securities, and interest income. The same principle may sometimes be applied to summaries of property accounts and depreciation. On the other hand, we sometimes observe some fanciful arrangements of analyses, ostensibly designed as labor-saving devices, that must have taken more time to figure out than would have been consumed in expressing the facts in a simpler manner.

A judicious use of distinctive ticks and colored pencils will often be found helpful, as designations regarding procedure in the verification of accounts, but care should be exercised to furnish a key to the significance of such designations.

As a rule, analyses should not be abstracted from previous papers and used again. However, this is sometimes desirable to avoid rewriting lengthy explanations, and may be done provided a memorandum is placed in the previous papers, properly indexed, to show where the paper can be found.

Too much emphasis cannot be laid upon the necessity for an accountant's including in his working papers everything that comes to his attention bearing upon the audit. He should make notes of any conclusions he may reach regarding the accounts, and make them complete enough so that, to take an extreme case, but one with which we have had to deal recently, if he were to die before the report is prepared some one else could prepare it from his papers. In brief, the accountant should bear constantly in mind that his working papers are the only record of what he has done, and that for this reason there should be a complete record, including any conclusions or deductions he may have arrived at—both for his own use, during the work and after its completion, and for the use of others.