

10-1986

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### Recommended Citation

Kelley, Timothy and Seiler, Robert E. (1986) "Audit Time Budgets: A Cost-Benefit Analysis," *Woman C.P.A.*: Vol. 48 : Iss. 4 , Article 5.

Available at: <https://egrove.olemiss.edu/wcpa/vol48/iss4/5>

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# Audit Time Budgets

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## A Cost-Benefit Analysis

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By Timothy Kelley and Robert E. Seiler

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Time budgets are useful tools for scheduling the various parts of an audit engagement and for optimal assigning of personnel to these activities. Larger CPA firms usually expend considerable effort in setting and monitoring time budgets and in some cases even utilize computer programs to insure optimal scheduling of tasks and people. In smaller practices, such sophisticated methods may not be utilized; nevertheless, there must be some method, either formal or informal, of establishing target times for the completion of the identifiable stages of an engagement.

Time budgets are two-edged swords. They provide benefits to both client and practitioner, but they also carry a cost. Since the benefits which time budgets provide are somewhat more obvious than the costs, this article is directed primarily toward the cost side of the cost-benefit equation. The purpose of the discussion is to provide data concerning (1) the impact that these time budgets have on persons who actually perform the engagement and (2) the perceptions of auditors about the causes of time-budget stress. Hopefully, the data will help CPA firms minimize the cost of time budgeting, which appears primarily in the form of reduced enthusiasm, increased frustration and stress, and, in some cases, termination and turnover of personnel.

A cost-benefit analysis is, in essence, a weighing of benefits against costs and the deciding upon a particular course of action should the benefits be greater than the costs. The following list illustrates the imbalance which should be achieved between the costs and benefits of utilizing audit time budgets. The list shows that the benefits outweigh the costs, tipping the scale in favor of utilizing time budgets. If the

time budgets are not properly administered, however, the costs may become excessive, thus altering the balance.

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### Time-Budget Costs

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Job stress  
Turnover  
Clerical record keeping  
Errors (deliberate or unintentional)

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### Time-Budget Benefits

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Manpower planning  
Job sequencing  
Fee setting  
Performance evaluation  
Determining slippages  
Planning future engagements

### The Benefits

An enumeration of the benefits to be derived from careful division of the engagement into definable activities would be of value in our assessments of the costs. The benefits spring from the preparation of a plan showing the manhour forecast for the completion of each audit activity. A time budget would thus be set for the cash work, receivable confirmations, inventory observation, vouching, and any similar activity in the engagement which has separable time requirements for completion. These estimated time requirements provide the basis for improved planning in the following areas:

**Manpower assignments.** To insure that persons with the right amount of expertise are available at the right time for each activity.

**Sequencing.** To insure the proper scheduling of any activity that must be completed before another is begun.

**Fee Setting.** To insure that fees are in line with the amount and type of work required.

Monitoring the actual time spent on each activity and comparing it to

the original budget provides additional control information. Some of the areas which are strengthened with this feedback information are:

**Performance evaluation.** The performance of individual persons can be measured, and those who consistently meet the time estimates are identified as well as those who are not.

**Schedule slippages.** If the engagement is falling behind the original schedule, this fact can be highlighted sooner and the *extent* of the slippage can also be better gauged. This knowledge permits better communication with clients concerning expected timing of work and rescheduled completion dates.

**Setting future time budgets.** The planning of future engagements, and the resultant fees, can be more accurately planned.

### The Costs

These benefits cannot be obtained without a cost. Obviously, the amount of time spent on different clients must be separately maintained for billing purposes, but a breakdown of time spent on each separate activity is another matter. The task of matching actual time with the original budget is primarily an *internal* planning and control function, and it is in the performance of this function that stress and anxiety are produced. Audit personnel, especially staff and seniors, bear the brunt of maintaining and reporting time on individual activities; when actual time is matched against the time budget as input to the performance evaluation process, the amount of stress can be enormous. Fear of not meeting a time budget for a particular activity creates sufficient stress to necessitate that the firm's management exercise constant vigilance to insure accurate reporting of time and to prevent shifting of time from one activity to another. In extreme cases, where performance evaluation is heavily dependent upon meeting time budgets, some auditors might work overtime and not report this time on their time report or even might sign off on an audit program step without performing the work. In summary, the advantages of using detailed time budgets can be realized only at the risk of producing behavior which is dysfunctional to the firm, to the firm's personnel, and to the client.

## Time-Budget Pressures

Research was recently conducted within the profession to determine (1) the extent of time-budget pressures that auditors face, (2) the causes of these pressures, and (3) potential strategies for reducing these time-budget pressures. A questionnaire designed to probe these matters was sent to two hundred auditors in the Houston and Los Angeles areas. Auditors associated both with large firms and with local and regional firms were included, and a total of 91 usable responses were obtained (a 45% response rate). Participants were selected so that an approximately equal number of replies would be received from partners, managers, seniors, and staff auditors. The responses indicate that seniors are more affected by time-budget pressure, with partners, managers, and staff experiencing almost equal but lower levels of time-budget stress. Table I reflects the proportion of the respondents at each organizational level that found time budgets to be (1) tight and practically unattainable, (2) attainable with considerable effort, (3) attainable with reasonable effort, or (4) very easy to attain.

A generally recognized principle of budgeting, which is well documented in behavioral theory, is that a budget should be "tight but attainable." If it is too loose, there is little incentive to increase one's effort because it can easily be achieved. If it is too tight, there is also a loss of incentive because "it is impossible to achieve anyway, so why try?" If audit time budgets are either too loose or too tight, there will undoubtedly be dysfunctional consequences.

Table I shows that respondents reported that 48% of the audits they had worked on in their present job position had time budgets that required considerable effort to attain (13% plus 35%), while 52% of their time budgets could be reasonably attained or were easy to attain (44% plus 8%). However, one of the most striking figures reflected in Table I is the fact that seniors reported budgets to be practically unattainable 27% of the time. This percentage is almost three times the magnitude reported by other groups, and is undoubtedly a reflection of the responsibilities

and duties of seniors which make them particularly vulnerable to budget pressure. For the most part, seniors are the ones who must assign specific tasks to staff, select audit samples, review the work to insure that all audit steps are completed, and, in general, assume responsibility for the completion of the field work. They are also in a position where time-budget performance is an important element in the evaluation of their work.

These figures lead to speculation on the impact that this very heavy time pressure has on the turnover rate within the profession. Studies have shown that turnover at the senior level is much higher than at other points in the public accounting career ladder. The complexities of the factors that produce high levels of turnover do not permit direct conclusions in this regard from the data presented here, but future research of a behavioral nature that probes the relationship between time-budget pressure and turnover would be of value to the profession.

A second question in this research probed the perceived causes of the high level of time-budget pressure when it occurred. Table II reports the reasons given by respondents. They are listed in the order of frequency in which they were mentioned. By far, the greatest amount of pressure is produced by tying the time budget to the fee estimate given the client. Once a fee is established, the pressure to complete the work within the time permitted by that fee can be quite intense. Time estimating (second on the list) and planning the audit (fourth on the list) are both within the control of the personnel of the CPA firm, but the third item on the list, lack of client cooperation and unanticipated problems with the records, is not. The last three items on the list were of far less magnitude than the other perceived causes of budget pressures. A conclusion may be warranted that a significant portion of the time-budget pressures are produced by policies or actions of the public accounting firm and are thus due to factors within the firm's control.

The questionnaire included one inquiry about possible solutions to the problem of time-budget pressures. These responses are shown

in Table III. The three most frequently mentioned solutions were better planning, improved communication within the CPA firm, and avoidance of tying time budgets to fees. These answers are, for the most part, compatible with the causes of stress shown earlier. Better planning and better communication within the firm accounted for almost half the proposed solutions (21 of 49 responses), and these solutions are feasible, even when budgeted time and fees continue to be linked.

The nine respondents who suggested that firms refrain from tying time budgets to fees were all managers and seniors. They indicated that CPA firms should establish reasonable time budgets even in those situations where the firm expected to "write off" and thus not bill the client for some of the hours expected to be worked on the audit. In other words, these auditors suggested that the firm should consciously absorb the cost of low billings and communicate this decision to the audit field personnel. In this way, the pressure on seniors or managers to work overtime but not report some of these hours on their time reports would be removed.

## Conclusions

In a cost-benefit analysis, one weighs the benefits against the costs to determine whether a particular course of action should be undertaken. Audit time budgets that have detailed time allotments for each aspect of the engagement will have benefits in excess of costs, provided that the time budgets are used in such a manner that dysfunctional behavior rarely occurs.

According to many of the auditors in this study who reported the existence of tight time-budget pressures, the cost of time budgets may be minimized through better planning and communication within the firm. Following these suggestions, the extent to which meeting the budget will enter into the performance evaluation process should be clearly communicated, especially to seniors who experience greater amounts of budgetary pressure. Another possible method of lessening the cost side of the picture is a more careful distribution of time-budget allotments to each segment of the engagement,

**TABLE I**  
**Time-Budget Difficulty Experienced By Auditors**

% of the Time That Budgets Were Considered	Partners	Managers	Seniors	Staff	All Respondents Combined
Very tight, practically unattainable	9%	10%	27%	8%	13%
Attainable with considerable effort	39	34	29	40	35
Attainable with reasonable effort	44	45	38	45	44
Very easy to attain	8	11	6	7	8
	100% (N = 25)	100% (N = 22)	100% (N = 21)	100% (N = 19)	100% (N = 87)

\*These statistics reflect the arithmetical means of the aggregate responses by auditors to the question, "What percentage of the audits that you have worked on in your present job position have had budgets that were (1) very tight, practically unattainable, (2) attainable with considerable effort, etc.?" Of the 91 respondents, 4 did not answer this question.

**TABLE II**  
**Perceived Causes of Time-Budget Pressures**

	All Auditors (No. of Responses)
(1) Client fee pressures	42
(2) Poor/optimistic time estimating	21
(3) Lack of client cooperation/unanticipated problems with client records	20
(4) Poor planning of audit	19
(5) Overemphasis on rewarding "making budget"	5
(6) Underreporting of chargeable hours by prior year's audit team	4
(7) Overestimate by staff of the importance of "making budget"	4
<b>TOTAL RESPONSES</b>	<b>115*</b>

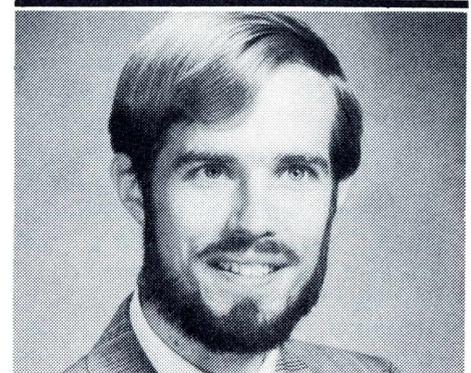
\*Some respondents listed more than one cause of time-budget pressures.

**TABLE III**  
**Proposed Solutions to the Problems of Time-Budget Pressures**

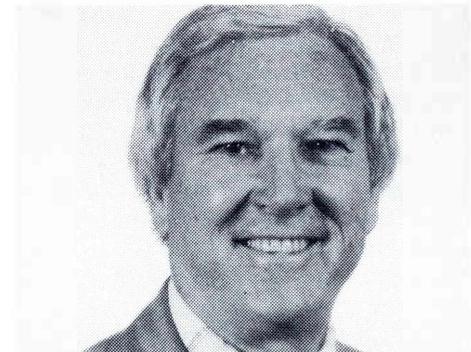
	All Auditors (No. of Responses)
Better planning to establish reasonable budgets	11
Improve communication within CPA firms	10
Stop tying budgets to fees	9
Better communication with client	5
Pessimistic — see no solution to problems	5
Improve efficiency of audits	4
Stop price cutting to obtain new clients	3
More ethics and professionalism	2
<b>TOTAL NUMBER OF RESPONSES</b>	<b>49</b>

\*This table reflects responses to an open-ended question asking for "suggested solutions" to the problem of time-budget pressures in public accounting firms. Only the respondents who perceived that time-budget pressures were a significant problem for the profession (54% of all respondents) answered this question.

with participation to the extent possible by those who must meet the time budgets. This would prevent perceptions by those doing the field work that the time budget is "unattainable" to begin with. The time required in prior years' audits should be carefully reviewed before it is set as the basis for the current year's time budget. Errors in the prior year's time budget or in the clerical recording of time (either knowingly or inadvertently) should be searched out and corrected before the new time budget is set. These efforts will not only increase the benefits of time budgeting but will also considerably decrease the costs. □



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