Audit Sampling

Audit sampling is testing a sample out of a larger population of items for the purposes of forming an audit conclusion.

Example – Testing 90 invoices out of a population of 1,000's for appropriate approvals.

A properly selected sample enables the auditor to conclude on the likelihood of misstatement or the effectiveness of controls without testing the entire population of transactions.

Testing a sample does involve some amount of uncertainty because we are not testing 100% of the population. This is acceptable as long as the uncertainty is not too great and the cost of testing 100% outweighs the benefits.

This uncertainty is measured by various types of risk. As risk increases, sample sizes and the extent of audit procedures must also increase.

Sample Evaluation – Relates only to the likelihood that misstatements or deviations from controls are included in the audit sample on a proportionate basis to the rest of the population.

Evaluating evidence obtained through sampling still requires judgment.

Audit Risk – Includes uncertainties due to sampling and factors other than sampling.

Sampling Risk – The risk the auditors conclusions from evaluating the sample are different than if the auditor evaluated the entire population.

When sample sizes are small, sampling risk is high.

Allowance for Sampling Risk = Tolerable Rate – Expected Rate

Alternative formula = Upper Precision Limit – Actual Rate

Economics 2 – Business Cycles

Whether the economy is growing or shrinking is determined by several factors, including interest rates, taxes, government spending, and the money supply. The money supply determines whether we have inflation or deflation. Inflation and deflation affect how and when businesses and consumers decide to spend.

Aggregate Demand (National) – The demand curve for an entire country.

> Aggregate demand curves shift if participants in the domestic economy change spending behavior due to interest rate changes, wealth changes or foreign exchange changes or if demand for exports overseas changes

Gross Domestic Product (GDP) – Measure of the size of an economy.

> Includes all final goods and services in a country produced by domestic and foreign sources
>
> It excludes common stock. When GDP is rising, the economy is expanding. When GDP is falling, the economy is shrinking

Government Purchases – Increased purchasing increases aggregate national demand.

Aggregate Supply (National) – The supply curve for an entire country. Generally, it is shaped like a hockey stick – flat with a 45 degree ramp as quantities increase and the overall economy nears peak production capacity.

Nominal – The current price or cost of an item.

Real – Price or cost adjusted for inflation.

Gross Domestic Product (GDP) – The sum of the price of all goods and services produced by a country during 1 year. Can be calculated based on all incomes earned associated with producing goods and rendering services or based on expenditures to purchase goods and services.

Pension

Defined Contribution (401(k) Plan) - The amount contributed by the employer or employee is fixed, but the payout at retirement is not. Employers expense contributions as incurred.

Defined Benefit (Pension Plan) - The payout upon retirement is fixed.

2 Defined Benefit Plan Entities - Employer that supports the pension and the pension plan itself.

Employer Entries	Pension Plan Entries
Pension expense	Projected benefit obligation
Deferred pension cost	Plan assets
Prepaid or accrued pension cost	Vested benefits
Minimum pension liability	Accumulated benefit obligation
Net loss not recognized as pension expense	
Unrecognized past service cost	
Unrecognized gains/losses	

Pension Expense - Unrelated to cash contributions. Recognize expense over the period of employee's employment (the service period).

Business Structure

Sole Proprietor – An individual engaging in a business.

No federal or state filings are required but proprietor may decide to make a fictitious name filing

Not a separate legal entity

Capital is limited to owner's funds

Simplest business structure

General Partnership – Has 2 or more partners.

Treated as a pass-through entity for tax

Written articles are not required

Cannot be a not-for-profit

General Partner – Manages the partnership and has unlimited personal liability.

Can be a general partner and limited partner at the same time

Limited Partnership – Must have at least 1 general partner.

Death of a limited partner does not cause dissolution of partnership

Limited Partner – Partner in a partnership whose liability is limited to the extent of his/her share of ownership.

If a limited partner acts like a general partner and a 3rd party does not know the partner is a limited partner, the limited partner has unlimited liability relative to dealings with that 3rd party

Can act as an agent of a partnership or vote on removal of a general partner without losing limited liability