

# Contents

<i>Preface</i>	vii
<b>1 The uses of statistical sampling in auditing</b>	<b>1</b>
Introduction	1
The five sampling methods	2
Discovery sampling	3
Acceptance sampling	4
Estimation sampling of attributes	5
Estimation sampling of variables	6
Monetary unit sampling	9
Summary	9
Question series 1	9
Some answers to question series 1	10
<b>2 Some terms used in statistical sampling</b>	<b>11</b>
Some brief definitions	11
Some terms used in statistical sampling	12
<b>3 The basic theory of sampling</b>	<b>13</b>
A practical example	13
The level of confidence	14
Using the sample to test a hypothesis	17
Using the sample proportion as a best estimate	19
What size of sample?	19
Standard error of the sample mean	20
The standard error of other statistics	23
A comment on the 'actual' error rate	23
Question series 3	24
Some answers to question series 3	25
<b>4 What size of sample does the auditor need?</b>	<b>26</b>
Introduction	26
On calculating an optimal sample size	26
The effect of population size on sample size	30
<u>What level of confidence does an auditor need?</u>	<u>31</u>
<u>The precision limit</u>	<u>32</u>

Confidence level versus precision limit	33
Summary	34
Question series 4	34
Some answers to question series 4	35
<b>5 How to measure the standard deviation of accounting populations</b>	36
Introduction	36
The concept of dispersion	36
The conventional method of calculating the standard deviation of a population	39
A speedier way of calculating standard deviation	40
Finding the standard deviation of large populations	41
Average range method of estimating standard deviation	42
The effect of standard deviation on sample size	43
The coefficient of variation	44
Summary	45
Question series 5	45
Some answers to question series 5	46
<b>6 Methods of drawing a random sample</b>	47
Introduction	47
What is a sample?	47
Drawing the sample	47
Random sampling with and without replacement	48
Judgement versus random sampling	48
The advantages of random sampling	49
The pure random sample	49
The systematic random sample	50
Junior digit random sampling	51
Other methods of random sampling	52
Testing for randomness	53
The 'run' method of testing for randomness	53
Testing larger populations	55
Summary	56
Question series 6	56
Some answers to question series 6	57
<b>7 Some comments on defining and analysing an accounting population</b>	58
What is a population?	58

Attributes and variables	58
On defining accounting populations	59
The meaning of homogeneity	60
The meaning of skewness	61
How do we measure the skewness of a population?	63
Using the median instead of the mode	64
Mode or median?	65
The problem of stratification	65
Stratifying debtors, inventory and other value populations	65
The optimal stratification plan	66
Example of stratification	68
Stratification in practice	70
Other strategies for stratification	72
The Lorentz curve	73
Question series 7	73
Some answers to question series 7	75
<b>8 Estimation sampling of values (variables) and proportions</b>	
<b>(attributes)</b>	78
Estimation sampling of variables	78
Calculating sample size using formulae	80
Estimating the value of differences	81
Ratio estimates	84
Difference versus ratio estimates	86
Ratio versus simple random sampling of checked population	86
A caution	86
Estimation sampling of attributes	86
A note on joint confidence limits	90
Summary	90
Question series 8	91
Some answers to question series 8	92
<b>9 <i>Acceptance and discovery</i> sampling</b>	94
Glossary of abbreviations used in acceptance sampling	94
Introduction	94
Acceptance sampling	94
The mechanics of acceptance sampling	96
The case of the 'hardline' policeman	97
The double sampling approach	100
Sequential sampling	101

Which acceptance sampling plan is the best?	102
Discovery sampling	103
The case of the overworked doctor	103
Practical example of discovery sampling	105
Summary	106
Question series 9	107
Some answers to question series 9	108
<b>10 Cluster, multistage and replicated sampling</b>	<b>109</b>
The cluster sample	109
How do we calculate the precision limit on a cluster sample?—variable sampling	110
Cluster sampling for attributes	112
Summary	113
Multistage sampling	113
A general method of calculating sampling error	118
Question series 10	120
Some answers to question series 10	123
<b>11 Sundry topics</b>	<b>125</b>
Introduction	125
One tailed tests, confidence level and sample size	125
A caution on one tailed tests	127
Some additional comments on the average range method of calculating standard deviation	128
On treating several populations as one	132
On checking several populations from the same sample	132
A random sample is a random sample is a random sample	134
The problem of the missing voucher	135
The finite population correction factor	135
Estimating the size of populations	138
On calculating the level of confidence in previous years when statistical sampling not employed	139
Graphs versus tables	140
What does the auditor do if the audit fee is insufficient to cover the required sample size?	141
Using statistical sampling to test systems	142
Using the computer to assist in sampling	143
Sample size and the interim audit	144
Question series 11	145
Some answers to question series 11	147

<b>12</b>	<b>The detection of fraud</b>	149
	Introduction	149
	Levels of significance	149
	The needle in a haystack problem	150
	The 'Salami type' fraud	151
	Summary	153
	Question series 12	153
	Some answers to question series 12	154
<b>13</b>	<b>Case study on statistical sampling in auditing—verifying the provision for doubtful debts</b>	155
<b>14</b>	<b>Statistical cost allocation</b>	162
	Introduction	162
	The cost allocation problem	162
	The traditional allocation procedure	163
	Manual versus machine methods	163
	Statistical cost allocation	164
	The mechanics of statistical cost allocation	165
	Level of confidence	165
	Example	166
	Some other examples	171
	Conclusion	173
	Question series 14	174
	Some answers to question series 14	174
<b>15</b>	<b>Can the Bayesian approach assist the auditor?</b>	176
	Introduction	176
	Subjective probability	176
	Objective probability	178
	Testing a doubtful debts provision	179
	Using Kraft's tables to calculate level of confidence	183
	What has the Bayesian approach achieved?	183
	Question series 15	185
	Some answers to question series 15	187
<b>16</b>	<b>Some advice on integrating statistical sampling into conventional auditing procedures</b>	188
	Introduction	188
	1. Ensure informed support from the top	189

2. Ensure that informed opinion about scientific sampling is provided at every level of the firm	190
3. Must we have access to a fully qualified statistician when designing the sampling plan?	191
4. How do we select the first application?	192
5. When you apply scientific sampling to an audit for the first time prepare a job manual, detailed audit programme and procedure booklet	195
6. Other points to consider	197
7. The need for a library	198
Summary	198
Question series 16	199
Some answers to question series 16	199
<b>17 Monetary unit sampling</b>	<b>200</b>
Introduction	200
A description of the MUS system	200
The method of deciding on the reliability factor	201
The method of deciding on monetary precision	203
Calculating the sample size	206
Type of error	208
Example	208
The discovery of monetary error	209
Adjusting the MP for monetary error	209
Adjusting for compliance error	211
Example	213
A worked example of the MUS system	214
Final estimate of adjusted MP	218
The advantages of monetary unit sampling	218
Operational advantages	219
Theoretical advantages	219
Limitations of the MUS system	220
Question series 17	224
Some answers to question series 17	225
<b>18 Some statistical sampling tables available</b>	<b>226</b>
Introduction	226
Description of sampling tables available	226
<b>19 A summary of the formulae</b>	<b>228</b>
Introduction	228

<b>20</b>	<b>A selective bibliography on statistical sampling in auditing</b>	<b>232</b>
	Books on the general theory of sampling	232
	Books on applying sampling to auditing and accounting	232
	Articles	233
<b>21</b>	<b>Tables and Graphs for calculating sample size plus set of instructions for operating each system</b>	<b>236</b>
	Sampling table index	236
	Areas under the normal curve	237
	Discovery sampling tables	238
	Estimation sampling of attributes	239
	Estimation sampling of variables (values)	249
	Acceptance sampling	257
	Method of constructing other single sampling plans	261
	Instructions for calculating a double sampling plan	264
	Average range method divisors for estimating the standard deviation of accounting populations	265
	Random numbers	266
	Finite population correction factor	270
	Random days	271
	Random weeks	271
	Random months	272
	<i>References</i>	273
	<i>Author Index</i>	275
	<i>Subject Index</i>	277