

Chapter 18

THE AUDIT OF PAYABLES

Many of the audit steps that are carried out on the payables balance are similar in principle to those that were carried out with receivables balances.

Note, however, that the auditor will be particularly worried about the possible understatement of payables: how can the auditor detect a payable that is missing from the financial statements?

- It's important to reconcile the individual payables balances to the control account. In other words, the total of payables in the balance sheet of the financial statements agrees to the detailed amounts payable to each supplier.
- Correspondence with suppliers and board minutes may allow identification of disputes or amounts which might not be paid, or amounts which may not yet appear in the payables ledger, but which are been claimed by suppliers or other parties. It's often by reviewing correspondence in board minutes that contingent liabilities are discovered. Contingent liabilities arise because of some event which has already happened, but whose outcome is uncertain. For example, a legal claim. Later you will see how contingent assets and contingent liability should be handled.
- Trace from orders to credits in suppliers' accounts. Trace from credit entries in the accounts to copy invoices then back to orders.
- Trace from cash book payments (before and just after year end) to suppliers' accounts and vice versa.
- The payables period would be looked at with some interest. If the payables period increases, it may indicate that the company is being more careful about when payments are made, but it could indicate that the company is having a difficulty making payments as they become due and by increasing the payables period, the company might begin to lose out on receiving cash discounts. This can become quite expensive of the company and need some explanation.
- On some occasions payables circularisations will be carried out. That's where we write to suppliers and ask them to confirm the amount that we owe. However, this is not as important as a receivable circularisation because very often payables balances would be substantiated by statements received from suppliers which can then be reconciled or agreed to balance on the supplier's accounts.
- Looking at payments made shortly after year end will often give evidence of the existence of a liability at year end.
- A review of credit notes received or debits made to payables accounts just after year-end is important. There may be some situations where a company wants to reduce its apparent profit in a particular year and one way in which this could be done will be the debit in expense account in a nominal ledger and credit a supplier, and then early in new the year reverse that transaction. So looking at transactions made at just after year-end can be very important in verifying the validity of transactions made just before year-end.

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