

# **Auditing Developments**

---

9<sup>th</sup> Edition

Steven C. Fustolo

# Table of Contents

---

<b>Section 1 – General Developments</b> .....	<b>1</b>
Learning Objectives .....	1
Introduction.....	1
Implications of the Current Economic Environment—Economic Issues Peculiar to Auditors.....	1
The Seeds Are Sown During the Good Times! .....	2
Accounting and Auditing Issues Related to the Coronavirus (COVID-19).....	20
General .....	20
Audit Issues to Consider with the Coronavirus.....	20
Review Questions.....	30
Review Answers .....	32
Client and Employee Fraud.....	34
General .....	34
<i>Report to the Nations on Occupational Fraud and Abuse</i> .....	34
Review Questions.....	45
Review Answers .....	46
Types of Fraud .....	47
Small Business Fraud .....	55
Evaluating an Entity’s Fraud Environment.....	59
Review Questions.....	64
Review Answers .....	65
Time Theft .....	67
Employee Background Checks and Credit Reports .....	68
The Auditor’s Role in Dealing with Fraud.....	68
Specific Fraud Issues.....	74
Anti-Fraud Measures .....	84
Sentences for Fraudsters.....	85
A Fraud Scorecard.....	87
Computer Crime and Theft.....	88
Integrity Survey.....	89
Correlation between Bankruptcy and Fraud.....	90
The CFO Perspective on Their Outside Auditors and Fraud .....	91
Madoff and the Single Auditor Issue .....	91
Criticism of Auditors Who Do Not Detect Fraud .....	93
Review Questions.....	95
Review Answers .....	96
<b>Section 2 – Auditing Developments</b> .....	<b>99</b>
Learning Objectives .....	99
Introduction.....	99
Attempting to Limit Auditor’s Liability .....	99
The Viability of the Big Four .....	107
Report of the Advisory Committee on the Auditing Profession to the U.S. Department of the Treasury .....	108
The Current Risky Environment for the Big Four .....	109
Pressure to break up Big Four .....	111
The Effect of Enron—19 Years Later.....	111
Sarbanes-Oxley Push to Record and Disclose Off-Balance Sheet Transactions.....	112
Going-Concern Issues .....	114
Background—Going Concern in Auditing Literature.....	114
Review Questions.....	116
Review Answers .....	117
Retaliation Against Auditors Who Issue Adverse Opinions .....	119
AICPA’s Top Technology Initiatives.....	119
Emerging Technologies .....	119

## Table of Contents

Anti-Sarbanes-Oxley Continues After 18 Years .....	120
Companies Have Lost Important Advisors.....	125
Some European Companies are Delisting from the U.S. Exchanges .....	125
Smaller Companies are Fed Up and Going Private: .....	125
Board Members are Concerned about Sarbanes-Oxley and Now Dodd-Frank.....	127
The Continued Trickle-Down Effect of Sarbanes-Oxley on Nonpublic Entities.....	129
CFOs Want to Change Sarbanes-Oxley.....	132
The Impact of Dodd-Frank on Auditors into 2020 .....	133
SEC Focuses On Missing Disclosures .....	136
SEC Conflict Minerals Disclosures .....	136
Whistleblowing—The New Profession Acts Like the Oldest Profession.....	138
Auditor Rotation.....	142
Review Questions.....	144
Review Answers .....	146
Peer Review .....	148
Recurring Peer Review Comments .....	148
Current Measurement Standards .....	152
Recent Developments in Peer Review .....	153
Review Questions.....	155
Review Answers .....	157
<b>Section 3 – Accounting and Auditing in Volatile Times.....</b>	<b>159</b>
Learning Objectives .....	159
Introduction.....	159
Key Focus Areas for the Auditor.....	159
Inquire as to the Status of Concentrations of Customers and Suppliers .....	159
Pay Attention to Key Financial Ratios and Analytical Procedures .....	159
Check for Going Concern.....	160
Check Loan Covenants and Restrictions.....	161
Be Aware of Client Pressures to Reverse Allowance and Reserve Accounts.....	161
Inventory Obsolescence.....	161
Impairment Issues—Real Estate .....	161
Watch Out for Round-trip Transactions .....	162
Look for Games Being Played with Expenses .....	162
Check for “Slush-Fund” Reserves and “Rainy Day” Funds and Distorted Estimates.....	162
Look at Underfunded Pensions and Post-Retirement Benefit Obligations .....	163
Auditors May Wish To Assist Clients in Tightening Operations .....	163
Watch Out for Related Party Transactions.....	164
Review Questions.....	166
Review Answers .....	167
Lessons from Litigation .....	168
Common Pitfalls for Accountants .....	168
Top Ten Actions to Minimize the Risk of Being Sued.....	171
Review Questions.....	180
Review Answers .....	181
Efficient Engagements—Reduce Time, Make More Money without Increasing Risk.....	183
Staffing Problems .....	183
Efficiency Auditing .....	185
Avoiding the Time Trap of Prepaid and Accrued Expenses .....	189
Practice Issues Relating to Auditing .....	190
Engagement Letter .....	190
Inventories.....	190
Confirmation Procedures .....	195
Auditing Cash .....	196
Auditing Cash-Basis Financial Statements .....	197
Legal Letters.....	198
Unusual Reporting Issues.....	199

## Table of Contents

Issuing Comfort Letters to Client Lenders.....	200
Management Representations Regarding Prior Periods Presented That Were Audited by the Predecessor Auditor .....	203
Signing and Dating Audit Reports—Naming the City and State Where the Auditor.....	204
Study on Public Perception of Accountants in Jury Trials.....	204
Review Questions .....	206
Review Answers .....	208
AU-C 265—Communicating Internal Control-Related Matters Identified in an Audit .....	210
Definitions.....	211
Considerations Specific to Smaller, Less Complex Entities.....	211
Existence of Compensating Controls.....	213
Communication of Other Deficiencies in Internal Control to Management.....	214
No Material Weakness Communications.....	214
Watch Out for the DOL and Audits of Employee Benefit Plans .....	216
Assessing the Quality of Employee Benefit Plan Audits—DOL Report.....	218
Why Do Individuals Cheat and Commit Fraud? .....	220
The Remorse Factor.....	221
The Isolated Fraudster Is More Susceptible to the Conditions in Fraud Triangle .....	221
Signing at the Beginning of a Document—Decreasing Dishonest Self Reports .....	222
Conclusions from the Study .....	222
Results and Discussion.....	223
Client Deadline Concentration in Audit Offices and Audit Quality.....	228
Results of the Study.....	228
Auditing Standards Board (ASB) Agenda .....	229
PCAOB and SEC Approve Naming Engagement Partners in Audit Engagements .....	229
Auditor-Provided Tax Services.....	230
ASB’s Six-Point Plan to Improve Audits.....	231
Review Questions.....	233
Review Answers .....	235
<b>Section 4 – Recent Auditing and Attestation Standards .....</b>	<b>237</b>
Learning Objectives .....	237
SAS Nos. 134–139 and SSAE No. 19 .....	237
SAS No. 134: <i>Auditor Reporting and Amendments, Including Amendments Addressing         Disclosures in the Audit of Financial Statements</i> .....	237
Review Questions.....	253
Review Answers .....	254
SAS No. 135: <i>Omnibus Statement on Auditing Standards—2019</i> .....	256
SAS No. 136: <i>Forming an Opinion and Reporting on Financial Statements of Employee         Benefit Plans Subject to ERISA</i> .....	257
SAS No. 137: <i>The Auditor’s Responsibilities Relating to Other Information Included in         Annual Reports</i> .....	263
Review Questions.....	267
Review Answers .....	268
SAS No. 138: Amendments to the Description of the Concept of Materiality.....	270
SAS No. 139: Amendments to AU-C Sections 800, 805, and 810 to Incorporate Auditor Reporting Changes from SAS No. 134.....	271
SSAE No. 19: Agreed-Upon Procedure Engagements .....	279
Review Questions.....	281
Review Answers .....	283
<b>Glossary.....</b>	<b>285</b>
<b>Index .....</b>	<b>289</b>