

Chapter 2—cont'd

Examples of errors:

--mistakes in gathering or processing accounting data

--incorrect accounting estimates from misinterpretation of facts

--mistakes in application of accounting principles

- greed or preoccupation with being successful**
- living beyond one's means**
- high personal debts**
- high medical bills**
- poor credit or inability to obtain credit**
- unexpected financial needs**
- personal financial losses**
- expensive habits such as the use of drugs, alcohol, or gambling**
- illicit sexual relationships**
- work-related pressures such as low pay, failure to receive a promotion, etc.**
- boredom**
- challenge to see if one can beat the system**
- spouse or family-related pressures**

- lack of segregation of duties**
- failure to inform employees about company rules**
- rapid turnover of employees**
- constantly operating under crisis conditions**
- lack of an audit trail**
- ineffective supervision**
- lack of transaction authorizations**
- poor accounting records**
- lack of physical controls**
- lack of access to information**
- breakdown of procedures**
- inappropriate computer access**

- feeling of being underpaid**
- belief of being overworked**
- feeling that “everybody else is doing it”**
- belief that rank has its privileges**
- attitude of low self-esteem**
- desire to seek revenge**
- outlook that it is only a loan and will be paid back**
- belief that nobody will get hurt**
- assumption that it is only temporary until operations improve**

- inability to generate cash flows from operations while reporting earnings and earnings growth**
- significant pressure to obtain additional capital necessary to stay competitive considering the financial position of the entity**
- assets, liabilities, revenues, or expenses based on significant estimates that involve unusually subjective judgments or uncertainties**
- significant related-party transactions**
- significant, unusual or highly complex transactions especially those at year end that pose difficult substance over form questions**
- significant bank accounts or subsidiary or branch operations in tax-haven or money-laundering jurisdictions for which there is no business justification**
- overly complex organizational structure involving unusual or numerous legal entities**

- difficulty in determining the organization or individual who controls the organization**
- unusually rapid growth or profitability**
- high vulnerability to interest rates**
- high dependence on debt**
- unrealistically aggressive sales or profitability incentive programs**
- threat of imminent bankruptcy or takeover**
- poor or deteriorating financial position when management has personally guaranteed significant debt of the entity**

**Accounting policies and procedures—
the auditor may conclude that there is a
risk of fraudulent financial reporting that
requires the auditor to consider further
management’s selection and application
of significant accounting policies**

**Controls—when a risk of material
misstatement due to fraud relates to risk
factors that have control implications,
the auditor’s ability to assess control
risk below the maximum may be reduced**

- consider the implications for other aspects of the audit**
- discuss the matter and the approach to further investigation with an appropriate level of management that is at least one level above those involved and with senior management**
- suggest that client consult with counsel**