

FLORIDA GULF COAST UNIVERSITY

ACG 4632 – INDEPENDENT AUDIT 1

FALL 2004

- Instructor:** Carl Pacini, Ph.D., J.D., C.P.A., C.F.S.A.
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- Website:** <http://ruby.fgcu.edu/courses/cpacini>
- Office Hours:** Mondays & Wednesdays: 10 am–12 noon
Tuesdays & Thursdays: 10-11 am
- Classroom :** Griffin Hall-Room 215
- Class Times :** Monday 5 pm-7:45 pm
- Last Day to Withdraw :** October 29, 2004
- Final Exam Date :** To be announced
- Required Materials :** 1) Modern Auditing, 7th edition, by Boynton, Johnson & Kell
2) Contemporary Auditing: Issues & Cases, 5th edition,
by Michael Knapp
- Suggested Materials :** CPA Exam Review Manual For Auditing
- Prerequisite :** ACG 3401 with a minimum grade of C and ACG 3113
with a minimum grade of C

YOU ARE EXPECTED TO READ AND UNDERSTAND THE CONTENTS OF THIS SYLLABUS. IT IS VERY POSSIBLE THAT I COULD ASK YOU AN EXAM QUESTION THAT IS BASED ON MATERIAL IN THIS SYLLABUS.

**Course
Background
(using a
Strategic Audit
Systems
Approach) :**

Accounting plays a central role in the efficient allocation of resources in market-based economies. By adding credibility to accounting measurements and disclosures, auditing has for centuries made it possible for accounting to play such a role. Today's global economy and the business organizations operating within it, however, have become so complex and interdependent that new approaches to auditing must be developed.

The traditional "risk based" audit focuses the auditor's assessment of risk through a narrow "accounting lens" – a lens that directs his or her attention, and his or her related assessment and testing activities to the nature of account balances, classes of transactions, and properties of the client's accounting system for the purpose of assessing the risk that financial statements are materially misstated. This "bottom up" focus can inhibit the auditor's development of the level of business understanding needed to effectively judge the risk of material misstatements in the financial statements.

The use of a "top down," aggregative, strategic systems lens increases the likelihood that the auditor will have obtained a sufficient understanding of the client's business and industry for the purpose of conducting a financial statement audit. The strategic systems audit approach directs the auditor's attention to the client's system dynamics: its business strategy and the economic niches it has chosen to occupy; the strengths of its connections to outside agents, including customers, suppliers, investors, and regulators; and the external and internal forces that threaten the viability of its chosen niches and the achievement of its objectives.

One example of the strategic systems audit approach is the Business Measurement Approach (BMP) used by KPMG Peat Marwick. The BMP audit approach is a holistic, business-risk orientation. It guides the focus, breadth, and depth of the auditor's knowledge acquisition and the integration of business knowledge into expectations about financial statement assertions.

**Course
Objectives:**

To provide knowledge of the societal significance of auditing, the legal and professional responsibilities of the CPA to clients and third parties and the nature of generally accepted auditing standards

To provide an understanding of audit planning and program development, audit risk and materiality considerations, and the significance of the various kinds of evidence examined during an audit in support of an audit opinion

To gain an understanding of the significance of internal controls in planning and performing an audit

To gain an appreciation of the Internet and other databases, such as Lexis-Nexis, Edgar and Research Insight, for auditors

To help prepare each student for the CPA, CMA, CIA, CFSA or CFE exam(s)

To gain an appreciation of assurance services

To apply auditing concepts and procedures to real cases to obtain a better understanding of auditing practices

To gain an understanding of basic fraud examination concepts

To learn planning and analytical skills and communication skills

**Program
Outcomes :**

This course is designed to help the student achieve the following outcomes:

To encourage and promote critical thinking, a skill necessary to succeed today as an accounting professional. This means each student should be able to comprehend an unfocused set of facts, identify, and if possible, anticipate problems, and find acceptable solutions.

To improve the student's communication skills. Each student should be able to locate, obtain, and organize information from both human and electronic sources. Each student will also learn to defend his or her views through written work.

To enhance the student's interpersonal skills. Cooperative learning or working in teams is one key way of promoting achievement of this outcome.

To promote a sense of professional skepticism and promote a spirit of willingness to investigate anomalous situations when rendering professional accounting and assurance services.

**Core
Competencies:**

In addition to the program outcomes noted above, this course promotes the following core competencies:

Acquisition of a global perspective by each student to help their future employers (or their own businesses) better compete in international and domestic markets;

Development of an ability to formulate decisions that integrate practical, economic and ethical considerations; and

Appreciation of the vagaries and uncertainties of real life business situations and the importance of life-long learning.

ATTENDANCE AND PARTICIPATION

Attendance and completion of assignments are considered minimum requirements for all students. Penalties may be assessed in the final determination of your course grade for unreasonable deficiencies in either or both of these requirements. The penalty may take the form of a reduction in letter grade, the assignment of a failing grade or a grade of incomplete. This penalty assessment policy applies regardless of performance on written examinations and the form of the penalty is at the discretion of the instructor.

Please note that 70 points toward your final grade involves attendance. Each student starts the semester with 70 points for attendance. Each time you miss class after one absence you lose 7 points from your attendance grade. The instructor retains the discretion to approve excuses on a case-by-case basis. If you miss class for a medical reason, do not ask the instructor to be excused without written documentation from a medical doctor or nurse practitioner. Participation in FGCU team athletic events is also a reasonable excuse for missing class.

Grading : Each student starts this class with an A. It is your job to keep it.

Two exams will be given in this course. Each exam will consist of objective questions and possibly short-answer essays. The second exam may be cumulative. It is assumed that each student will remember the material already learned that is necessary to answer a given question. Each student's grade will be based on the following:

Exam 1	100 points
Exam 2	100 points
Bell Manufacturing Case	75 points
SHS Case	75 points
Homework	80 points
Attendance/Participation	<u>70 points</u>
TOTAL	500 points

The grading scale for final grades is:

<u>Grade</u>	<u>Total Points</u>
A	460-500
A-	445-459
B+	435-444
B	415-434
B-	395-414
C+	385-394

C	350-384
D	300-349
F	Below 300

Any grade challenge to a test, case, homework assignment or project must be in writing to be considered. An oral or verbal grade challenge will not even be considered. A written grade challenge must clearly describe what is being challenged and provide a rational basis for the challenge.

Make-up exams will not be given without the instructor's approval. If you miss an exam without a reason approved by the instructor, you may receive a "0". The instructor's discretion is final. If you hand in the AAER project or a homework assignment late, you may have points deducted from your grade.

Please bear in mind that you are responsible for all material assigned even if it is not covered in a class lecture. You are also responsible for material presented in class that is not covered in the textbook. You are also responsible for any outside reading material assigned by the instructor. IT IS ALMOST CERTAIN THAT YOU WILL BE ASSIGNED MATERIAL TO READ OUTSIDE CLASS. QUESTIONS ON THIS MATERIAL MAY SHOW UP ON AN EXAM.

Homework Assignments:

Numerous cases from *Contemporary Auditing: Issues and Cases* and various AAERs will be covered in this course. Each student is responsible for writing out the answers to assigned case and/or AAER questions for class. You do not have to turn in answers to end-of –chapter questions but you should be ready to discuss your answers in class. The maximum number of points for any given assignment is 10. You must do at least one AAER out of the eight homework assignments. You may receive up to 80 points from homework assignments. The cases and AAERs that are the subject of homework assignments are listed in the Schedule of Assignments. **ALL HOMEWORK ASSIGNMENTS ARE TO BE WORD-PROCESSED. HANDWRITTEN ASSIGNMENTS WILL NOT BE ACCEPTED.**

Accounting & Auditing Enforcement Releases (AAERs)

The SEC Accounting and Auditing Enforcement Releases describe cases of fraudulent financial reporting. In many of these cases, the auditor is disciplined because of a failure to meet professional standards. The AAERs provide students a unique opportunity by presenting real-world auditing problems and how they are dealt with by the SEC. One source for the AAERs since September, 1995, is the Edgar database maintained by the SEC at www.sec.gov. Another source is Lexis-Nexis at library.fgcu.edu.

Questions to be considered in your written analysis should include:

1. What auditing deficiencies were there in this case?
2. What is the proper accounting based on the facts?
3. What were the red flags?
4. What should the auditor have done differently?

Auditing Team

Projects:

Teams of auditing students (no more than 4 on a team) will complete two cases, Bell Manufacturing, Inc. and Student Health Services (SHS). Each case is worth 75 points.

In Bell Manufacturing, student audit teams must resolve a fictitious yet realistic ethical dilemma. You assume the role of audit manager in a large, national CPA firm. You will be presented with a scenario whereby you learn from the CFO that he entered the US and worked a number of years under false pretenses for the audit client (Bell) while he was an illegal alien. Although the CFO recently obtained US citizenship, subsequent audit work revealed that Bell failed to obtain the documents required under federal law to certify his eligibility for employment. You will be required to electronically search the authoritative literature covering illegal acts by a client, as well as standards on fraud and the Code of Professional Conduct. Researching the authoritative literature is a requirement for the new CPA exam. Completion of this case will contribute to development of your ethical, analytical, research, and communication skills, better preparing you for practice and the new CPA exam.

Student Health Services (SHS) is a nonfictional case of employee fraud in a university setting designed to expose students to several different fraud issues. Topics covered in this case include an explanation of why people commit fraud; the profile of the typical fraud perpetrator; recognizing red flags that may indicate the presence of fraud; the importance of a strong system of internal controls in preventing and detecting fraud; and audit procedures that may help detect a skimming scheme.

Schedule of Assignments:

	<u>ASSIGNMENT</u>
Ch. 1 Auditing and the Public Accounting Profession	1-21, 1-22, 1-23 & 1-28
<u>Case</u> – Laurel Valley Estates	All questions
Ch. 22 Assurance Services	22-12 & 22-13
<u>Case:</u> Yale Express System, Inc.	All questions

Ch. 2 Financial Statement Audits and Auditors' Responsibilities 2-18, 2-19, 2-20 & 2-21
Case – Livent, Inc. All questions

Various materials on fraud examination and basic fraud concepts (including a discussion on SAS 99 – Consideration of Fraud in a Financial Statement Audit)

Outside readings: Beasley, M.S. 2003. SAS No. 99: A New Look at Detection of Fraud. *Journal of Forensic Accounting* IV (1): 1-20.

Krambia-Kardis, M. 2002. A Fraud Detection Model: A Must for Auditors. *Journal of Financial Regulation and Compliance* 10 (3): 266-278.

Grove, H. and T. Cook. 2004. Lessons for Auditors: Quantitative and Qualitative Red Flags. *Journal of Forensic Accounting* V(2): 131-146.

All outside readings are available on the course website at ruby.fgcu.edu/courses/cpacini. Questions from these articles may appear on Exam 1.

Ch. 3 Professional Ethics 3-23, 3-24 & 3-25
Case-Mallon Resources, Inc. All questions

AAER #192-Professional ethics-auditor received stock from the client firm. Extensive discussion of independence.

AAER #564-Professional ethics, independence, Evidence-fictitious assets and auditor-owned shares in an IPO.

Ch. 4 Auditor's Legal Liability 4-22 & 4-23
Case-National Student Marketing Corp. All questions
Case-Congregation of the Passion v. Touche Ross See below

You are to find this court case (Congregation of the Passion) in Lexis-Nexis or elsewhere (decided in the 1990s) and analyze the implications of the holding with regard to limitation of an accountant's liability to a client through the use of an engagement letter. Your analysis should not overlook the importance of SAS 83 and an article by Crawford, Franz, Zimmerman and Fink (use ABI Inform or other source) on this issue. You must do the research on your own to find the materials necessary to complete the assignment. **This assignment is worth up to 15 bonus points if you hand it in and it is substantially correct. Your project paper must be at least four pages double-spaced using 12 point font. It also counts as a homework assignment.**

Ch. 5 Overview of the Audit Process 5-17, 5-18 & 5-19
Case: Leslie Fay Companies All questions

EXAM 1—CHS. 1,2,3,4,5, and 22 and any outside material

Ch. 6 Audit Evidence, Audit Objectives, Audit Programs and Working Papers 6-22, 6-23 & 6-24
Case-Capital Banc Corp. All questions

Ch. 7 Accepting the Engagement and Planning the Audit 7-25, 7-26 & 7-27
Case-National Medical Transportation Network All questions

Outside reading: Wells, J.T. 2001. Irrational Ratios. Journal of Accountancy 192 (2): 80-3.

Ch. 8 Materiality, Risk and Preliminary Audit Strategies 8-24 & 8-25

AAER #1142-Due professional care and professional skepticism-materiality judgment related to reserves.

Ch. 9 Understanding Internal Control 9-32 & 9-34
(excluding Appendix 9A)
Case-Goodner Brothers, Inc. All questions

Ch. 20 Reporting on Audited Financial Statements 20-20, 20-21, 20-22 & 20-23

AAER #1207-the senior management of Power Phone, Inc. orchestrated a fraudulent scheme to falsify and inflate the firm's financial condition.

Ch. 21 Other Services and Reports 21-18, 21-19 & 21-20

EXAM 2 – Chapters 6, 7, 8, 9, 20 and 21 and any outside readings

The syllabus may be changed at the discretion of the instructor as circumstances warrant.

Ethics : Ethics have become an extremely important topic in today's environment. An accountant's only product is his/her service which is measured by his/her integrity and professionalism. It is expected that no academic dishonesty will occur. Cheating on any assignment will be pursued according to the appropriate procedures outlined in the Student Conduct Code. Cheating includes plagiarism on any of the assigned projects.

All students are expected to demonstrate honesty in their academic pursuits. The university policies regarding issues of honesty can be found under the Student Code of Conduct on page 11, and under

Policies and Procedures on pages 18-24 of the Student Guidebook. All students are expected to study this document which outlines their responsibilities and consequences for violations of the policy.

DISABILITY ACCOMMODATION SERVICES

Florida Gulf Coast University, in accordance with the Americans with Disabilities Act and the university's guiding principles, will provide classroom and academic accommodation to students with documented disabilities. If you need to request accommodations in this class due to a disability, or you suspect that your academic performance is affected by a disability, please see me or contact the Office of Multi-Access Services. The Office of Multi-Access Services is located in the Student Services Building, Room 214. The phone number is (239) 590-7925.