Completing the Audit

Preparation Questions

1. A ____________________________ is a potential future obligation to an outside party for an unknown amount resulting from activities that have already taken place.

2. ____________________________ include such things as agreements to either purchase raw materials or sell products at set prices to certain companies.

3. At the completion of the audit, management is typically asked to make a written statement as a part of the letter of ________________ that it is aware of no undisclosed contingent liabilities.

4. In a standard client's attorney letter, the attorney is requested to communicate about contingencies up to the date of ____________________________.

5. The auditor's responsibility for reviewing for subsequent events is normally limited to the period beginning with the date of the ____________________________ and ending with the date of the ____________________________.

6. When the auditor uses one audit report date for normal subsequent events and a later date for one or more subsequent events that come to the auditor's attention after the end of fieldwork, the audit report is said to be ____________________.

7. A potential legal claim against a client where the condition for a claim exist but no claim has been filed is referred to as a(n) ________________ claim.

8. Subsequent events that require adjustment to the financial statements provide additional information about significant events or conditions that did not exist at the date of ____________________________.

9. Subsequent events that require an adjusting entry are said to have ________________ on the financial statements.

10. Subsequent events that require disclosure are said to have ________________ on the financial statements.

11. The purpose of an unadjusted misstatement audit schedule is to determine if ____________________________ .

I. Introduction:

   Phase IV: Completing the Audit

   - Presentation and disclosure (what would the reader want to know?):
   - usually integrate with cycle testing
   - occurrence and rights and obligations – did happen
   - completeness – no footnote omitted
II. Review for Contingent Liabilities and Commitments

A. Contingent Liability

1. Definition –
   a. depends on future outcome (versus a liability).
   b. Important to auditor due to responsibility for fair presentation and disclosure.
   c. SASs require searching for and considering.

2. Conditions (for an activity that has already taken place)
   a. Potential future payment/impairment
   b. Uncertainty about the amount
   c. Be resolved in the future

3. Levels of likelihood (Table 24-2):
   a. Probable
      * reasonably estimate → record
      * cannot estimate → disclose
   b. Reasonably possible → disclose
   c. Remote → do nothing for now

4. Evidence needed:
   * that indicates existence of possible loss
   * on likelihood of unfavorable outcome
   * on amount of potential loss

5. Procedures
   * Discuss with management (inquiry)
     * status of prior year contingent liabilities
     * current year contingent liabilities
     * subsequent year contingent liabilities
   * Get management’s written representations
   * Review minutes
   * Review legal invoices
   * Obtain letters from attorneys
   * IRS correspondence, etc.

6. Inquiry of Attorney (Figure 24-2) – ask response to be dated near expected date of audit report.

7. Attorney’s statement
   * Asserted claims (existing claims)
* Unasserted claims (confidential)
* Impair confidentiality
* Disclose a secret
* Prejudice defense of claim
* Constitute an admission
  o SOX requires reporting of violations.

8. Auditor’s follow-up responsibility \(\rightarrow\) modify report, if uncertain full disclosure

B. Commitments – footnote significant agreements.

III. Subsequent Events
A. Importance – SAS 1: responsible for fair presentation and disclosure

B. Terms
  1. **Review for subsequent events** – responsible to search for through end of fieldwork (audit report date).
  2. **Subsequent discovery of facts** – not responsible to search for, comes to our attention after completion of fieldwork.

C. Subsequent events may either require:
  1. Adjustment (direct effect on F/Ss)
  2. Disclose (indirect effect)
  3. Revise/recall (should have known)
  4. Do nothing

Choose  
1, 2, 4  
3, 4

Dec. 31  Feb. 20  March 2  
Year end  Fieldwork  Issue report

D. Procedures
  1. Inquiries of management
  2. Attorney correspondence
  3. Subsequent interim financial statements
  4. Subsequent records
  5. Subsequent minutes
  6. Letter of representation (from management)

E. Report dating for discovery of subsequent event
  1. Extend **ALL** testing to new date
  2. Use dual dating of report
IV. Final Evidence Accumulation
A. Perform final round of Analytical Procedures.

B. Consider entity’s ability to continue as a going concern (AU 341)

C. Obtain client’s representation letter (AU 335)
   - signed by president, CFO.
   - on company letterhead.
   - dated as of audit report date.
   - PCAOB Standard 5: Responsibility for Internal Controls

D. Consider information accompanying basic financial statements (AU 551)

E. Read other information in annual report (AU 550)

F. Complete various checklists.

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Look at financial statements → consider evidence →
choose type of report → issue audit report

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V. Additional Communications
A. Report ALL fraud and illegal acts to audit committee (SAS 99).
B. Significant deficiencies and material weaknesses discovered in the internal control system (in writing) to those charged with governance.
C. Auditor responsibility, scope and timing, significant findings, and relevant information to those charged with governance.
D. Management letter – list recommendations for improvements.