



THE AUDITOR'S REPORT

Volume 33, No 3
Summer 2010

AUDITING SECTION / AMERICAN ACCOUNTING ASSOCIATION

Report of the President

Urton Anderson



It has certainly been an interesting decade to be a student of the auditing profession this past decade. The decade began with the audit of financial statements as "loss-leader" for public accounting firms, saw a cataclysmic change in the structure of the profession with Sarbanes-Oxley and the creation of the PCAOB, experienced another wave of corporate scandals and a constitutional challenge to the PCAOB, and ended with The Supreme Court going to great lengths to

preserve Sarbanes-Oxley and the PCAOB.

To put the importance of the Court's decision in perspective I quote the June 28 joint statement by former Congressman Michael Oxley and former Senator Paul Sarbanes:

The PCAOB provides essential protections to the more than half of American households that invest savings in securities. It ensures the integrity of public company audits and, thereby, the accuracy of financial reporting. The PCAOB enjoys widespread support from investors as well as from the accounting profession. The decision from the Supreme Court adjusts the law in a way that allows the PCAOB to continue to ensure the integrity of public company audits. The Board's essential protections of American investors will continue.

As reminder of just how big a change has taken place, I refer you to the excellent article in *Current Issues in Auditing* by Bill Gradison and Ron Boster, "The PCAOB's First Seven Years: A Retrospection," (Volume 4, Issue ,1 2010, Pages A9–A20), available at the Section's website.

The decade's changes and challenges to the auditing profession are certainly reflected in the extensive and dynamic program that Kenny Reynolds and Karla Johnstone have put together for the 2010 AAA

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Meeting in San Francisco. I don't recall ever seeing so many sessions – my quick count of the preliminary program indicates 50 session with two or more auditing papers and 10 panel sessions on auditing topics. In addition to these sessions we will also have Berry Salzberg, CEO of Deloitte for the section's luncheon speaker on Monday.

Audit Boot Camp

Thirty-five participants attended our Second Audit Educator's Bootcamp which was held June 15-17 at DePaul University. As in prior years the demand exceeded the number of spots and we had to close registration prior to the deadline. Reports from participants again rated the program as extremely valuable. Thanks to Jay Rich and Ray Whittington for their excellent work in planning and coordinating the event and to Frank Buckless, Scott Showalter, and Jay Thibodeau for instructing.

We have heard from a number of you that you need the date set earlier so that you can plan your summer activities. We are planning to have a Third Bootcamp next summer in Chicago, probably about the same time period in June. This year we will try to get the date set in early September.

Strategic Plan for the Section

As reported in our last news letter, the Executive Committee, in conjunction with support from AAA, has begun a formal strategic planning process. This effort is being led by Steve Glover, who will assume the Section's Presidency August 2, and Scott Showalter, our new Vice President/Academics and President Elect. In addition to the current executive committee members (Shaun Budnik, Audrey Gramling, Chris Hogan, Linda McDaniel, Jay Thibodeau, and myself) several members from the section-at-large were asked to join the Section's Strategy Team. These members are Brian Ballou (Miami University), Mark Beasley (North Carolina State), Jeff Cohen (Boston College), and Ray Whittington (DePaul University). Dale Karren and Jan Brown from Petrous have provided excellent facilitation and support for the process.

We began the formal process in March and have made excellent progress using the framework and process provided by Petrous. This has included numerous conference calls and a two day meeting held June 9 and 10. To date the strategy team has done a thorough analysis of the section's current status; identified strengths, weakness and opportunities; clarified the section's value proposition, developed a vision and a mission statement; and set out five strategic initiatives. Currently we are in the process of developing specific action steps to implement these strategic initiatives along with specific measureable goals and timelines. We hope to complete this part of the process in August and have the plan ready for role out to the section prior to the January Midyear Meeting in Albuquerque.

Executive Committee Changes

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Fall 2010 Issue Deadline

The deadline for material to be included in the Fall 2010 issue of *The Auditor's Report* is September 30, 2010. The preferred format is a Word file attached to an e-mail message. We are also open to any proposals for materials that anyone would like to submit. Please send all material and proposals to the incoming Editor at the address below by September 30, 2010, to ensure timely publication of the issue:

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At the August AAA meeting Audrey Gramling (Past-President), Jay Thibodeau (Secretary), Shaun Budnik (Vice President/Practice), and Linda McDaniel (Historian) will rotate off the executive committee. I wish to thank each of these individuals for the work they have done for the section and their willingness to extend their efforts beyond their term as they continue the work on the section's strategic plan and its implementation.

I would also like to welcome the newly elected officers of the section. They are:

D. Scott Showalter, Professor of Practice, North Carolina State University
- VP Academic

Walton Conn, Global Head of Audit Methodology and Implementation,
KPMG LLP - VP Practice

Jennifer Joe, Associate Professor of Accountancy, Georgia State
University – Secretary.

Scott has already been heavily involved with the section these past few months as he and Steve Glover have been leading the section's strategic planning efforts.

People to Serve on Nominations Committee

Following the recent change in the Section's by-laws, we are announcing a call for nominations for the 2010 – 2011 Nominating Committee. Please consider nominating yourself or another member of the Auditing Section. The Nominating Committee's duties include soliciting candidates from the membership for open offices and preparing a slate of at least one candidate for each of the open offices. Consider becoming involved in selecting the next leaders of the Auditing Section. Additional details on the by-laws change, and the responsibilities of the nominating committee, are [available online](#). Nominations for the Nominating Committee should be submitted to Audrey A. Gramling by **July 15, 2010**, at agramli1@kennesaw.edu.

2011 Auditing Section's Midyear Conference in Albuquerque

Even though you haven't gotten to the AAA Annual Meetings yet, it is not too early to plan for your submission of papers and panel sessions for the 2011 Midyear Meeting to be held January 13-15 in Albuquerque New Mexico. Program co-chairs Scott Vandervelde and Mike Wilkins are already at work in setting up plenary speakers and will soon be soliciting papers and proposals for panel sessions. So while you are talking with your colleagues in San Francisco and come up with that perfect session, let Scott and Mike know about it.

Finally, our section gives out numerous awards at our Midyear Meeting, but the selection process starts in a few weeks. The information about the awards and how to make a nomination can be found at <http://aaahq.org/>

[audit/awards.htm](#). The Section gives awards in research, education and service to the auditing profession. Consider nominating a colleague, mentor, teacher, PhD student or even yourself. Nominations are due July 15, 2010.

I will end by noting what a great privilege it has been to serve as the Section's President this past year. I continue to be amazed by the extent of the dedication so many of you members have shown to the work of the section in its mission to further the auditing profession through research and teaching. This certainly includes the members of the executive committee, the committee chairs and vice-chairs, editors, and the committee members; but also the membership as a whole. Whenever tasks need to be done, I never had to look far before finding someone to step up. I, however, would like to express my special thanks to Audrey Gramling and Steve Glover. To Audrey, for excellent job she did over her past three years as Vice President/Academic, President, and Past President. The discipline, organization and order she brought to the section's operations will be a legacy to the section for the years to come. To Steve, for his willingness to undertake the leadership for the strategic planning, a monumental task.





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The path toward a single set of global auditing standards*

By Denise Esdon and Darrel R. Schubert**

Much has been written in the recent past about the need for a global set of high quality accounting standards that can be applied consistently by companies around the world. However, similar coverage has not been given to the growing need for a single set of global auditing standards that can be consistently applied by those auditing such companies.

The setting of auditing standards has traditionally been the domain of national standard setters, with a focus on the needs of local investors, capital market participants, regulators and others. Companies seeking to raise capital in a foreign country would, in many cases, be required to have their financial statements audited in accordance with that foreign country's auditing requirements. That way, the theory goes, local investors and other stakeholders would have confidence that the audit has been conducted in accordance with standards that they are familiar with and understand.

However, the globalization of capital markets has magnified the need for global auditing standards. Not only do investors want and need audited information that is comparable across companies in different countries, but it is reasonable to expect that they also will want to know that the quality of the audit is the same across jurisdictions. The move to International Financial Reporting Standards (IFRS) in many countries is expected to increase the comparability of financial reporting, enhancing investors' confidence in financial statements in different countries. A single set of high-quality global auditing standards are an important counterpart to global accounting standards. Global auditing standards can help enhance investor confidence on a global level and provide investors with a clearer understanding of the nature of the audit work undertaken – and the rigor involved – regardless of where the audit is performed.

Who should be the global auditing standard setter?

The International Auditing and Assurance Standards Board (IAASB) is designated by, and operating under the auspices of, the International Federation of Accountants. Its objective is to serve the public interest by setting, independently and under its own authority, high-quality standards and by facilitating the convergence of national and international standards. This objective contributes to enhanced quality and uniformity of practice in these areas throughout the world, and to strengthened public confidence in financial reporting.

The IAASB consists of a full time chair and 17 volunteer members from around the world. Board membership includes individuals in public practice with significant experience in the field of auditing as

well as an equal number of individuals who are not in public practice. The IAASB also has three official observers (from the US Public Company Accounting Oversight Board, the European Commission, and the Japanese Financial Services Authority) who have the right to speak at meetings.

The IAASB's rigorous due process reflects appropriate expertise and also involves transparent consultation and stakeholder engagement.

The IAASB is subject to the oversight of the Public Interest Oversight Board (PIOB). The objective of the PIOB is to increase the confidence of investors and others that the setting of standards by the IAASB is properly responsive to the public interest. Among its responsibilities, the PIOB ensures that IAASB standards are only issued after it has concluded that due process has been followed effectively and with proper regard to the public interest.

The IAASB also receives input on its agenda, project timetable, priorities and technical issues from a Consultative Advisory Group (CAG) representing regulators, business and international organizations and users and preparers of financial statements.

The structure and robust due process of the IAASB, with the oversight of the PIOB and the involvement of the CAG, position it as a global standard setter operating in the public interest. This governance model enhances the credibility and acceptability of the International Standards of Auditing (ISAs) as global auditing standards.

The International Standards on Auditing

The IAASB embarked on a program in the late 1990s designed to update and revise its "core" auditing standards (in particular, the risk assessment, fraud and the audit reporting ISAs). The revisions were viewed as necessary to the acceptance of the ISAs as high quality standards by regulators and national standard setters. The revisions took on added importance, and regulatory interest, in light of significant business scandals in the early 2000s.

In 2004, the IAASB started a comprehensive program to enhance the clarity of ISAs to make them more understandable and better capable of being interpreted consistently. This program involved the application of new drafting conventions to all ISAs either as part of a substantive revision or through a limited redrafting of the standards. The program was completed in February 2009, and auditors worldwide now have access to 36 newly updated and clarified ISAs, which are effective for audits of financial statements for periods beginning on or after December 15, 2009.

The clarified ISAs are designed to be more compatible with regulatory frameworks, facilitating the independent public oversight of auditors and providing a basis for promoting mutual recognition of inspection processes.

Over 120 countries are using or are in the process of incorporating the ISAs in their national auditing standards or using them as a basis for setting national auditing standards. The benefits of global standards are compelling and all national auditing standard setters should be encouraged to adopt the clarified ISAs as national standards. Where this is not possible, for example, when a legally established body is responsible for setting auditing standards, a process of convergence should be undertaken to enhance the consistency of audits in all jurisdictions.

Developments in the United States

Presently, audits in the US are conducted under somewhat different standards, depending upon whether the company being audited is private or public. While there has been some movement to align such standards with the ISAs, to date progress has been mixed.

Several years ago, the Auditing Standards Board (ASB) of the American Institute of Certified Public Accountants (AICPA), which sets the auditing standards for audits of non-public companies, adopted an International Convergence Plan. This plan stipulates that the ASB will adopt an official position of ISA BASE, which means that the ASB agenda will harmonize with the IAASB and new Statements on Auditing Standards (SASs) will use the ISAs as the base standard. At the same time, the ASB embarked on its own Clarity Project, which includes redrafting all of the existing auditing standards to make them easier to read, understand and apply. This project is well underway and the clarified SASs will be effective for audits of financial statements for periods ending on or after December 15, 2012.

Recently, the Public Company Accounting Oversight Board (PCAOB), which sets the auditing standards for audits of US public companies, has exposed or issued a number of new standards, such as the Risk Assessment suite of standards, Communications with Audit Committees and Engagement Quality Review. In each case, the PCAOB indicated that they considered the equivalent standards of the IAASB and the ASB in their drafting process; however, they have retained their own particular style and approach to writing standards. The PCAOB has included appendices in the latest proposed standards, comparing such proposals to the equivalent ISAs or SASs and discussing why they believe differences are appropriate. In many instances, such differences are more than trivial.

Summary

The needs of investors and financial statement users are best served by the existence of a single set of high-quality global auditing standards. While it may not be possible to completely achieve this goal in the near term, we believe that it is important that standard-setters establish a migration path that minimizes the need for jurisdictional differences and that financial statement users make their voices heard with those standard-setters.

**This column represents the views of the authors only, and does not necessarily represent the views or professional advice of Ernst & Young LLP.*

***Denise Esdon, partner of Ernst & Young's Global Standards, Methodology & Implementation, was Deputy-Chair of the IAASB from 2002 to 2008*

Darrel R. Schubert, partner of Ernst & Young's Professional Practice-Auditing, is the current chair of the AICPA Auditing Standards Board



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Fraudulent Financial Reporting: 1998-2007

By Mark Beasley, Joe Carcello, Dana Hermanson, and Terry Neal*

Executive Summary

COSO sponsored this study, Fraudulent Financial Reporting: 1998-2007, to provide a comprehensive analysis of fraudulent financial reporting occurrences investigated by the U.S. Securities and Exchange Commission (SEC) between January 1998 and December 2007. This study updates our understanding of fraud since COSO's 1999 issuance of Fraudulent Financial Reporting: 1987-1997. Some of the more critical findings of the present study are:

- There were 347 alleged cases of public company fraudulent financial reporting from 1998 to 2007, versus 294 cases from 1987 to 1997. Consistent with the high-profile frauds at Enron, WorldCom, etc., the dollar magnitude of fraudulent financial reporting soared in the last decade, with total cumulative misstatement or misappropriation of nearly \$120 billion across 300 fraud cases with available information (mean of nearly \$400 million per case). This compares to a mean of \$25 million per sample fraud in COSO's 1999 study. While the largest frauds of the early 2000s skewed the 1998-2007 total and mean cumulative misstatement or misappropriation upward, the median fraud of \$12.05 million in the present study also was nearly three times larger than the median fraud of \$4.1 million in the 1999 COSO study.
- The companies allegedly engaging in financial statement fraud had median assets and revenues just under \$100 million. These companies were much larger than fraud companies in the 1999 COSO study, which had median assets and revenues under \$16 million.
- The SEC named the CEO and/or CFO for some level of involvement in 89 percent of the fraud cases, up from 83 percent of cases in 1987-1997. Within two years of the completion of the SEC's investigation, about 20 percent of CEOs/CFOs had been indicted and over 60 percent of those indicted were convicted.
- The most common fraud technique involved improper revenue recognition, followed by the overstatement of existing assets or capitalization of expenses. Revenue frauds accounted for over 60 percent of the cases, versus 50 percent in 1987-1997.
- Relatively few differences in board of director characteristics existed between firms engaging in fraud and similar firms not engaging in fraud. Also, in some instances, noted differences were in directions opposite of what might be expected. These results suggest the importance of research on governance processes and the interaction of various governance mechanisms.
- Twenty-six percent of the fraud firms changed auditors between the last clean financial statements and the last fraudulent financial statements, whereas only 12 percent of no-fraud firms switched auditors during that same time. Sixty percent of the fraud firms that changed auditors did so during

the fraud period, while the remaining 40 percent changed in the fiscal period just before the fraud began.

- Initial news in the press of an alleged fraud resulted in an average 16.7 percent abnormal stock price decline in the two days surrounding the news announcement. In addition, news of an SEC or Department of Justice investigation resulted in an average 7.3 percent abnormal stock price decline.
- Long-term negative consequences of fraud were apparent. Companies engaged in fraud often experienced bankruptcy, delisting from a stock exchange, or material asset sales following discovery of fraud – at rates much higher than those experienced by no-fraud firms.

Given the small number of frauds examined in this study that involve time periods subsequent to the issuance of the Sarbanes-Oxley Act of 2002, further research will be needed once sufficient time has passed to allow for more observations of SEC fraud investigations involving post-SOX time periods before any conclusions can be reached about the effectiveness of that legislation in reducing instances of fraudulent financial reporting.

Our hope is that insights contained herein will encourage additional research to better understand organizational behaviors, leadership dynamics, and other important aspects of the financial reporting process that may have an impact on fraud prevention, deterrence, and detection.

We believe the results of this study will be useful to investors, regulators, stock exchanges, boards of directors, external auditors, and other key stakeholders as they seek to prevent, deter, and detect fraudulent financial reporting.

*The full report is available for free PDF download at <http://www.coso.org>.



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Committee Spotlight

By Jay C. Thibodeau, Bentley University

The Auditing Section of the AAA is successful because of the many members who agree to serve on one or more of the Section's committees. This column profiles the activities of one of the Section's committees. In this issue of *The Auditor's Report*, the Executive Committee is profiled.

The charge of the executive committee is to direct the affairs of the Section and carry out its programs in a manner that is consistent with the Section's mission statement. The executive committee is comprised of the President, Vice President-Academic, Vice President Practice, Treasurer, Secretary, Historian, and Past President. The President, Vice President-Academic, and Past President each serve one year terms. All other officers serve two year terms. The Vice President-Academic serves as the President after his/her one year term and then serves one more year as the Past President. The 2009-2010 Committee Members include:

Urton Anderson, President (University of Texas)
Audrey Gramling, Past President (Kennesaw State University)
Shaun Budnik, Vice-President, Practice (Deloitte)
Steve Glover, Vice-President Academic (Brigham Young University)
Linda McDaniel, Historian (University of Kentucky)
Chris Hogan, Treasurer (Michigan State University)
Jay Thibodeau, Secretary (Bentley University)

During the current year, among other activities, the executive committee has initiated the development of a robust strategic planning process. Our hope is that the process will help the Auditing Section in our quest to provide relevant thought leadership to the broader auditing profession. The expected outcomes of the process include the following:

1. **To provide the strategic direction for the section over the next three to five years.** We believe that such a direction will help to set the future course of the Auditing Section in motion. Importantly, our strategic planning process will be consistent and complementary with the overall AAA strategic plan.
2. **To establish the strategic framework for decision making.** We believe that the process will help to establish continuity between leadership teams, provide a process for initiating and sustaining multi-year efforts and create a pattern for leadership teams long into the future.
3. **To identify priorities and help evaluate incoming ideas from the membership.** We believe that the process will help provide the basis for officers to make decisions with a consistent focus

on the highest priorities of the section and our members.

4. **To help structure and guide executive committee meetings based on the strategic direction of the section.** We believe that the process will allow for highly productive executive committee meetings.
5. **To provide the basis for engaging colleagues throughout the Audit Section to participate in meaningful ways.** We believe that the process will help the committee determine the very best manner in which to assign representatives from the Auditing Section to important initiatives and committees.

We expect the strategic planning process to be dynamic and to evolve depending on the changing environment that we operate within. The process has been skillfully led by incoming Vice-President, Academic, Scott Showalter (North Carolina State University) and a consultant hired by the AAA, Dale Karren. In addition to the members of the Executive Committee, the following Audit Section Members have also generously worked on this critically important initiative:

Brian Ballou (Miami University)
Mark Beasley (North Carolina State University)
Jeffrey Cohen (Boston College)
Ray Whittington (DePaul University)

The Executive Committee will provide an update on the strategic planning process at this year's Annual Meeting in San Francisco. Until then, if you would like to learn more or share any ideas or suggestions, please feel free to contact any of the colleagues working on the initiative.



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PCAOB Update

By Martin F. Baumann, Gregory Scates and Dima Andriyenko*
Prepared for *The Auditor's Report* (Summer 2010)

Introduction

This update addresses selected PCAOB developments since the Spring 2010 Update that are likely to be of interest to accounting and auditing researchers, educators, and students. The developments discussed include: the proposed auditing standard on audit committee communications; the staff audit practice alert relating to significant unusual transactions; a meeting of the PCAOB Standing Advisory Group; the sixth annual PCAOB Academic Conference; a meeting of the PCAOB Investor Advisory Group; and the publishing of the list of issuer audit clients of non-U.S. registered firms in jurisdictions where the PCAOB is denied access to conduct inspections.

March 2010

Proposed Auditing Standard on Audit Committee Communications: The PCAOB proposed for comment an auditing standard on audit committee communications, and a series of related amendments to its interim standards on March 29, 2010. The proposal addresses requirements for auditors to communicate with audit committees of public company boards of directors. It considers a number of factors, including the importance of accounting judgments and estimates in financial reporting. The proposed auditing standard would supersede PCAOB interim standard AU sec. 380, *Communication With Audit Committees*, and AU sec. 310, *Appointment of the Independent Auditor*, and amend a number of other interim standards. The comment period on the proposed standard and amendments ended on May 28, 2010. The comments received on the proposal and other information related to this project can be found on the PCAOB website at: <http://pcaobus.org/Rules/Rulemaking/Pages/Docket030.aspx>

April 2010

Staff Audit Practice Alert No. 5: The PCAOB issued Staff Audit Practice Alert No.5, *Auditor Considerations Regarding Significant Unusual Transactions* on April 7, 2010 to remind auditors of public companies about their responsibilities to assess and respond to the risk of material misstatement of the financial statements due to error or fraud posed by significant unusual transactions. Practice Alert No. 5 complements Staff Audit Practice Alert No. 3, *Audit Considerations in the Current Economic Environment*, by further addressing risks of material misstatement associated with significant unusual transactions, risks that the staff believe continues to exist today. A copy of Practice Alert No. 5 can be found on the PCAOB

website at: <http://pcaobus.org/Standards/Pages/Guidance.aspx>

Standing Advisory Group (SAG) Meeting: The Board's SAG held its first meeting of the year on April 7-8, 2010. The meeting included a discussion of the PCAOB's current standard-setting activities and the recommendation from the Treasury's Advisory Committee on the Auditing Profession that the Board consider changes to the auditor's reporting model. PCAOB staff also updated the SAG on comments received on the proposed suite of risk assessment standards and sought SAG input on the standard-setting project on the responsibilities of the principal auditor. The meeting agenda, briefing papers, and meeting webcast can be found on the PCAOB website at: http://pcaobus.org/News/Events/Pages/04072010_SAGMeeting.aspx. The next meeting of the SAG is scheduled for Thursday, July 15, 2010.

PCAOB Academic Conference: On April 22-23, 2010, the PCAOB held its sixth annual Academic Conference, which was planned jointly by the staff of the PCAOB and members of the Auditing Section of the American Accounting Association. The conference was attended by 54 auditing researchers and educators, as well as PCAOB Board members and staff, FASB staff, and representatives of the U.S. Securities and Exchange Commission (SEC) and the U.S. Government Accountability Office. The conference, included a panel discussion with PCAOB Board members; presentations by and discussions with the leaders of the PCAOB Office of the Chief Auditor, Division of Registration and Inspections, Division of Enforcement and Investigations, and Office of International Affairs; presentations and discussions of two academic papers on topics related to the risk of fraud in financial reporting; and a separate discussion of the auditor's reporting model. The opening remarks of Dan Goelzer, acting Chairman of the PCAOB can be found on the PCAOB website at: http://pcaobus.org/News/Events/Pages/04222010_AcademicConference.aspx

May 2010

Inaugural Meeting of the Investor Advisory Group: The PCAOB held the inaugural meeting of the Board's Investor Advisory Group on May 4, 2010. The PCAOB created the Investor Advisory Group to provide a forum specifically for the Board to obtain the views of, and advice from, the broad investor community on auditor oversight matters affecting investors. The meeting agenda and other information can be found on the PCAOB website at: http://pcaobus.org/News/Events/Pages/05042010_IAGMeeting.aspx

List of Issuer Audit Clients of Non-U.S. Registered Firms in Jurisdictions where the PCAOB is Denied Access to Conduct Inspections: On May 18, 2010, the PCAOB published a list of more than 400 non-U.S. companies whose securities trade in U.S. markets, but whose PCAOB-registered auditors the Board currently cannot inspect because of asserted non-U.S. legal obstacles. The Sarbanes-Oxley Act of 2002 requires auditors to be registered with, and regularly inspected by, the PCAOB if they audit the financial statements that issuers file with the SEC. To date, the PCAOB has conducted more than 1,300 inspections of registered firms in the United States and 33 non-U.S. jurisdictions.

Because investors in U.S. markets may be relying on the audit work of certain firms without realizing that those firms are presently uninspected by the PCAOB, the Board published the list of issuers that have in 2009 or 2010 filed financial statements with the SEC that were audited by a firm in one of these jurisdictions. The auditors of these issuers appearing on the list are located in China, Hong Kong, Switzerland and 18 European Union countries. The PCAOB continues to work to eliminate obstacles to

inspections in these jurisdictions.

The list can be found on the PCAOB website at: <http://pcaobus.org/International/Inspections/Pages/IssuerClientsWithoutAccess.aspx>

* Martin F. Baumann is PCAOB Chief Auditor and Director of Professional Standards

Gregory Scates is PCAOB Deputy Chief Auditor

Dima Andriyenko is PCAOB Associate Chief Auditor



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Auditing Standards Board Update March 2010

Mark H. Taylor
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The Auditing Standards Board (ASB) convened one meeting since the spring update; the ASB met in Fort Worth, TX May 3-6, 2010. As has been typical, the meetings ran from Monday through Thursday afternoon and were open to the public. The agenda continued to be an ambitious one. This update provides highlights of the meeting's content and outcomes. If you have any questions regarding any of the ASB activities, please contact me at mt@case.edu.

1. Letters for Underwriters

Phil Wedemeyer, Chair of the Letters for Underwriters Task Force, led the ASB in a discussion of a revised draft of the proposed Statement on Auditing Standards (SAS), Letters for Underwriters. In consequence of the discussion, the ASB directed the Task Force to:

- Define requesting parties as "underwriters and other parties that are conducting a review process that is, or will be, substantially consistent with the due diligence process that would be performed if this securities offering were being registered pursuant to the Securities Act of 1933 (the Act).";
- Not distinguish parties with a statutory due diligence defense under section 11 of the Act from other requesting parties other than underwriters; and
- Not require legal opinions with respect to parties that have a statutory due diligence defense under section 11 of the Act.

The ASB also requested the Task Force to require the procedures included as application material in paragraph A63, and require that the comfort letter indicate if, at the client's request, the unaudited condensed financial information was attached only to the copy of the letter intended for the managing underwriter. A number of other issues were discussed that were primarily editorial in nature. The Task Force will bring a revised draft to the June 2010 meeting for vote to ballot for exposure.

2. Filings Under Federal Securities Statutes

John May, Chair of the AU Section 711 Task Force, led a discussion of Proposed Statement on

Auditing Standards Filings With the U.S. Securities and Exchange Commission Under the Securities Act of 1933. This agenda item was also discussed at the January 2010 meeting. Based on comments raised, the Task Force prepared a revised draft document in revising SAS No. 37, Filings Under Federal Securities Statutes (AICPA, Professional Standards, vol. 1, AU sec. 711), in accordance with the clarity conventions. There is no ISA that corresponds to AU section 711. The significant issues discussed follow:

- The proposed SAS requires the auditor to perform certain subsequent events procedures in proposed SAS Subsequent Events and Subsequently Discovered Facts, which includes separate definitions for subsequent events and subsequently discovered facts to clearly distinguish the auditor's responsibilities for each. The ASB directed the Task Force to add modifying language to the proposed SAS (paragraphs 7a, 10, and 12) to make it clear that the auditor is required to consider events occurring after the date of the auditor's report.
- Paragraph 7c of the proposed SAS contains a requirement for the auditor who has audited the most recent period for which separate audited financial statements of the entity are included in a registration statement to inquire or extend oral or previous inquiries of the entity's legal counsel. This requirement currently exists in paragraph 12 of SAS No. 1, section 560, Subsequent Events (AICPA, Professional Standards, vol. 1, AU sec. 560.12), and in paragraph 6 of SAS No. 12, Inquiry of a Client's Lawyer Concerning Litigation, Claims, and Assessment (AICPA, Professional Standards, vol. 1, AU sec. 337.06). However, proposed SAS Subsequent Events and Subsequently Discovered Facts ("proposed Subsequent Events SAS"), which clarifies AU section 560, changes this requirement. The proposed Subsequent Events SAS indicates that "the auditor may consider it necessary and appropriate to... inquire or extend previous oral or written inquiries of the entity's legal counsel concerning litigation, claims, and assessments...." Proposed SAS Audit Evidence—Specific Considerations for Selected Items ("proposed Audit Evidence SAS"), which clarifies AU section 337, also changes this requirement. The proposed Audit Evidence SAS, in paragraph 18, indicates that "If the auditor assesses a risk of material misstatement regarding litigation or claims that have been identified, or when audit procedures performed indicate that other material litigation or claims may exist, the auditor should ... seek direct communication with the entity's external legal counsel. ..." The ASB believes that the requirement in paragraph 7c of the proposed SAS to be more of a risk management concern and, therefore, directed the Task Force to change the requirement to application and other explanatory material to remain consistent with the respective approaches taken with the proposed SASs in the paragraph above.

The ASB unanimously voted to ballot the proposed SAS for exposure.

3. Association with Financial Statements

Dan Montgomery, Chair of the Auditor's Report Task Force, led the ASB in a discussion of AU section 504. The Task Force proposed that AU section 504 be withdrawn and its content addressed through conforming amendments to SSARS, to the extent needed, and in other SASs. The Accounting and Review Services Committee will be asked to consider the conforming amendments at its August 2010 meeting. The Task Force will bring a draft SAS containing the proposal to withdraw and the proposed conforming amendments to the ASB in July 2010.

4. Interim Financial Information

Brian Croteau, Chair of the Interim Financial Information Task Force (Task Force), led a discussion of the agenda materials. The Task Force has been charged with revising AU section 722, Interim Financial Information in accordance with the ASB clarity conventions.

- The ASB agreed with the revision to make the SAS applicable when the auditor audited the entity's latest annual financial statements and the appointment of another auditor to audit the current year financial statements is not effective prior to the beginning of the period covered by the review. Since the SSARS will be amended such that the SSARS will not be applicable in such circumstances, the ASB directed that SAS 116 be amended accordingly so that the revised applicability of SAS 116 and of the SSARS can be effective at the same time.
 - The ASB directed the Task Force to change the reference in the review report regarding the standards that the review was performed in accordance with from standards established by the AICPA to auditing standards generally accepted in the United States of America, to more specifically identify the relevant standards; to make the proposed SAS effective for reviews of interim financial information for interim periods of fiscal years beginning after December 15, 2012, to add reference in paragraph 7 to paragraphs 12-15 of proposed SAS Terms of Engagement; to revise the wording of paragraph 27 to more clearly state when a written report is required, and to make a number of other minor changes to the proposed SAS.
- The ASB voted unanimously to ballot the proposed SAS for exposure.

5. Subsequent Events

Sheila Birch, Chair of the Subsequent Events Task Force, led a discussion of the proposed SAS Subsequent Events (Redrafted). The objective was to discuss the significant issues identified in the comment letters received in connection with the exposure draft. The ASB directed the Task Force to:

- Include guidance related to situations in which a subsequent event disclosed in reissued financial statements can be labeled unaudited.
- Modify the definition of subsequent events to align more closely with the international standard.
- Maintain the requirements and guidance related to the predecessor auditor's responsibility for report reissuance in comparative financial statements within the proposed SAS.
- Add framework neutral guidance based on Technical Practice Aid TIS Section 8700.02, "Auditor Responsibilities for Subsequent Events."
- Determine the appropriate requirements and guidance within the proposed SAS to address the auditor's responsibilities related to litigation, claims, and assessments.
- The ASB also requested the Task Force to consider the application guidance related to dual-dating the auditor's report. Although the application guidance is consistent with International Standards, current practice is to dual-date the report with the same date as the subsequent event, and not the date the auditor completed the procedures in auditing the event.

The Task force will return to the July 2010 meeting with final changes in anticipation that the ASB will vote to issue the final standard.

6. Group Audits

Robert Dohrer, Chair of the Group Audits Task Force, led a discussion of the agenda material for proposed SAS Audits of Group Financial Statements (Including the Work of Component Auditors). The objective of the presentation was to discuss the significant issues identified in the comment letters received in connection with the exposure draft of the proposed standard. The ASB agreed with Task Force not to change auditor's report when dividing responsibility. Further, the ASB

discussed a concern that the approach in the proposed SAS to identifying significant components will lead to inefficiencies on multi-location audits because auditors are likely to take a “bottom-up” approach. The ASB directed the Task Force to consider developing application material to address this matters as well as application material to address group audits of smaller, less complex entities. Also, the latter will be addressed in the practice aid to be developed on group audits.

Additional discussion points follow:

- The ASB discussed the use of the term group engagement partner and the IAASB’s basis for conclusion for using that term rather than group auditor. Since certain requirements apply to the partner with final responsibility for the report, a distinction between the auditor who is the engagement partner and the other auditors on the engagement is necessary; the ASB concluded to retain the terminology used in ISA 600.
- The ASB discussed component materiality and directed the Task Force to develop more guidance on component materiality; including component materiality with respect to a referred-to component and how that differs from the materiality the group engagement team sets, and component materiality with respect to equity method investees.
- The ASB discussed whether significant components should be based on significant risks of material misstatements of the group financial statements or risks of material misstatement significant to the group financial statements, and whether the difference warrants divergence from ISA 600.

The Task Force will return with revisions at the July 2010 meeting in anticipation of voting to issue the final standard.

7. Quality Control

Sheila Birch, member of the Quality Control Task Force, led a discussion of the proposed SAS, Quality Control for an Audit of Financial Statements, and of the proposed Statement on Quality Control Standards (SQCS), A Firm’s System of Quality Control. The objective of the presentation was to discuss the significant issues identified in the comment letters received in connection with the exposure draft of these proposed standards.

SQCS, A Firm’s System of Quality Control

- The ASB directed the task force to add application material clarifying that although each element is required to have policies and procedures that are designed to provide reasonable assurance, whether a system of internal control is operating effectively may be assessed for the system as a whole.
- The ASB discussed the inclusion of the requirements related to engagement quality control review and made no changes and directed the task force to add application material addressing the assembly of final engagement files when no report will be issued.

SAS, Quality Control for an Audit of Financial Statements

- The ASB directed that the title as exposed be retained and the interim reviews be added to the first paragraph as an example of an engagement other than an audit conducted in accordance with generally accepted auditing standards.
- The ASB also required a revision to a reference in paragraph 2 to Governmental Auditing Standards to more accurately reflect what is incorporated in Governmental Auditing Standards, and the discussion in paragraph A7 about independence with respect to audits of governmental entities should be revised based on recent changes to Governmental Auditing Standards,

- The ASB also requested that a summary of the requirements specifically applicable to the engagement partner in this proposed SAS be included with the agenda materials when this proposed SAS is brought back to the ASB.

The Task Force will return with revised drafts at the ASB July 2010 meeting.

1. Special Reports

Rob Chevalier, Chair of the Special Reports Task Force, led a discussion of the materials for Agenda Item 8 Special Reports.

Special Purpose Frameworks

The ASB agreed with the Task Force to Limit the definition of special purpose frameworks to the four frameworks (cash, tax, regulatory, and contractual), as proposed. The ASB was silent on whether additional examples of such frameworks were needed. The ASB also did not conclude where the rationale for removing the category related to “the definite set of criteria having substantial support that is applied to all material items appearing in financial statements” could be provided. The ASB also agreed with the Task Force to not include the statement “Ordinarily, a modification would have substantial support if the method is equivalent to the accrual basis of accounting for that item and if the method is not illogical” as it relates to the definition of the cash basis of accounting. The ASB did not believe this would cause an inconsistency with Statement on Standards for Accounting and Review Services No. 19. The Task Force also recommended eliminating the new definitions related to regulatory basis statements (regulatory basis – general use statements and regulatory basis – restricted use statements), as the definitions caused more confusion. In this regard, the requirements and application guidance would also need to be modified to align with the language that was originally proposed, maintaining the requirements related to reports prescribed by law or regulation within the proposed SAS; however, the ASB requested the Task Force to include application guidance in the proposed SAS Forming an Opinion and Reporting on Financial Statements that references these requirements. A number of editorial changes were also discussed.

Single Financial Statements and Elements

The Task for proposed, and the ASB agreed with, the following:

- Maintaining the requirements and guidance related to audit procedures on interrelated items to obtain sufficient appropriate audit evidence about financial position, or financial position or results of operations.
 - Excluding a table of reporting requirements, similar to the proposed SAS Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks, as the table would be, in some respects, duplicative.
- A number of other minor changes were discussed and approved.

Summary Financial Statements

The Task Force recommended and the ASB approved the following changes:

- Including an additional objective related to the performance of procedures and also modifying the objective related to forming an opinion by clarifying the type of opinion to be expressed.

- Including the requirements in ISA 810, Engagements to Report on Summary Financial Statements, related to association within the proposed SAS.
- Broadening the proposed SAS to also apply to selected financial data and provide an example of such data, particularly related to the not-for-profit industry.
- Maintaining the form of auditor's opinion that the summary financial statements are consistent, in all material respects, with the audited financial statements from which they have been derived, as proposed.
- Maintaining the requirement for the audited financial statements to be "readily available," as that term has been defined in SAS 116 Interim Financial Information.
- The ASB also requested the Task Force to eliminate the reference to a "denial of opinion."

The ASB concurs with the form of opinion that it is inappropriate to, and the auditor does not, express an opinion; however, the ASB believes it is not necessary to introduce this new term within the auditing literature.

The Task Force will return to the July 2010 meeting with revisions to the Special Purpose Frameworks SAS and will bring final changes to the ASB on the Single Financial Statements and Elements SAS and the Summary Financial Statements SAS to the August 2010 meeting with the intention to vote to issue the final standards.

2. Related Parties

George Fritz, Chair of the Related Parties Task Force (Task Force), led a discussion of the comments received from the exposure of the proposed SAS, Related Parties, and the related revisions to the proposed SAS. Based on the comments received, the Task Force proposed, and the ASB agreed that:

- the definition of related parties as presented in the exposure draft is appropriate and that the related application material provides sufficient guidance with sufficient guidance with respect to GAAP frameworks as well as special purpose frameworks.
- the Task Force has appropriately provided guidance for auditors of governmental entities.

The ASB directed the Task Force to consider adding application material addressing considerations specific to auditing related parties of a governmental entity, and to make a number of other minor changes. The Task Force will bring a revised draft SAS to the ASB meeting in July 2010 to consider voting issue the SAS.

3. Auditing Accounting Estimates

Megan Zietsman, Chair of the Accounting Estimates Task Force (Task Force), led a discussion of the comments received from the exposure of the proposed SAS Auditing Accounting Estimates and the related revisions to the proposed SAS. The Task Force had not identified any issues for discussion by the ASB from the twenty-one comment letters received. The ASB reviewed the proposed SAS and had no substantive comments. The Task Force will bring the proposed SAS to the ASB for issuance as a final standard at its July 2010 meeting.

Concluding Comments

Three additional meetings are scheduled between the updates for which will appear in the Section's Fall newsletter: June (in Atlanta), July (in New Orleans) and August (in Denver). I encourage members of the Section to keep abreast of the numerous exposure drafts that have been or will be issued and to consider making a class project of preparing and submitting a comment letter on any of drafts. If you require additional information about the ASB and its activities, please contact me at mt@case.edu.



THE AUDITOR'S REPORT

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AUDITING SECTION / AMERICAN ACCOUNTING ASSOCIATION

GAO Update

by Jeanette Franzel & Maxine Hattery**

Serving Congress & the Nation: What's in Store for the Next 5 Years

As the audit and investigative arm of the U.S. Congress, the U.S. Government Accountability Office has oversight responsibilities that encompass the federal government, its service to the nation, and its role in the global community. While a single GAO engagement may drill deep into one program, that work is affected by national and worldwide trends. Strategic planning for GAO is a roadmap for its efforts, but it also offers a panoramic view of our government and the challenges we face as a nation. As in previous editions, *GAO's Strategic Plan: Serving the Congress and the Nation* for fiscal years 2010 through 2015 identifies trends that frame proposed goals and strategies.

Pressures to reduce the federal deficit are occurring as the nation is looking toward economic recovery. The need for analysis of programs and their effectiveness remains critical. Strategic financial management issues have taken on even greater importance as the federal government and the nation struggle with recovery act programs and issues. Fostering the improvements in the federal government's financial management and assurance will be critical in addressing GAO's strategic goals.

Identifying fraud, waste, and abuse has been raised to the level of a strategic objective with four performance goals: to perform forensic audits to identify and address vulnerabilities; conduct special investigations and security and vulnerability assessments; investigate allegations received through GAO's whistleblower hotline, FraudNET; and identify ways to strengthen accountability for the federal government's assets and operations.

At a time when the tension between environmental and energy needs could hardly be clearer, such issues receive strengthened emphasis in the revised plan. One of GAO's new performance goals is to "assess the nation's ability to ensure reliable and environmentally sound energy for current and future generations."

GAO invited comments on a draft of the plan from members of Congress and their staff; the Comptroller General's Advisory Board as well as other GAO advisory entities, which include representatives from the federal Inspector General, state and local government audit communities, and academia; GAO's sister agencies, the Congressional Budget Office, and the Congressional Research Service.

The plan comprises 4 strategic goals, 20 strategic objectives, 96 performance goals, and more than 300 key efforts. The following eight trends in the nation and the world have shaped GAO's goals and focus for serving Congress and the American people.

Trend: Evolving security threats

U.S. national security faces threats from global insecurity brought by the global recession; nuclear, biological, chemical, and other dangerous weapons; terrorism at home and abroad; regional instability in the Middle East, Afghanistan, Pakistan, and East Africa; and attacks on the U.S. information technology infrastructure.

GAO has also identified emerging threats brought on by competition for scarce energy resources and effects of climate change that could increase global poverty, social tensions, environmental degradation, and food scarcity.

To manage the demands of these threats, the government will need to develop new capabilities while under intense

pressure to reduce most federal agencies' budgets. GAO can play a useful role in evaluating long-term costs and trade-offs for restructuring U.S. capabilities.

Trend: Urgent fiscal sustainability and debt challenges

For more than a decade, each of GAO's fiscal simulations have shown the federal government to be on a path of unsustainable deficits and debt path due to spending pressures. One of GAO's fiscal simulations (which are based on historical trends and policy preferences) shows that if the federal government doesn't change its policies, debt held by the public as a share of national income or gross domestic product (GDP) could exceed the historical high reached in the aftermath of World War II by 2020—10 years sooner than the simulation showed just 2 years ago.

Challenges Affecting the Federal Budget in the Near Term

Year	Challenge
2008	Oldest members of baby-boom generation became eligible for early Social Security retirement benefits.
2008	Medicare Hospital Insurance (HI) outlays exceeded cash income.
2010	Social Security runs first cash deficit since 1984.a
2011	Oldest members of baby-boom generation become eligible for Medicare.
2014	45% of Medicare outlays funded by general revenue.b
2016	Social Security begins running consistent annual cash deficits.
2017	Medicare HI trust fund exhausted. Income sufficient to pay about 81% of benefits.b
2020	Debt held by public under GAO's Alternative simulation exceeds historical high reached in aftermath of World War II.

Source: GAO.
a - Based on Congressional Budget Office's (CBO) January 2010 baseline projections.
b - Based on 2009 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds (May 12, 2009). Projections showing the percentage of funding from general revenue reaching 45 percent by law trigger a "Medicare funding warning," requiring a proposal from the President in response.

GAO will continue to assist Congress by identifying opportunities to reduce spending; lower the risk of waste, fraud, abuse, and improper payments; identify areas for potential reform; narrow the gap between taxes owed and taxes collected; and fulfill its new mandate to assess duplication and overlap among federal programs and agencies. To help Congress monitor the government's financial and fiscal condition, GAO will continue to conduct financial statement audits and develop long-term fiscal simulations and analyses of federal deficits, federal debt levels, and the state and local sector.

Trend: Economic recovery and restored job growth

GAO staff have joined with their colleagues at other national audit institutions around the world to examine the causes of the national and global financial crisis and devise means to protect taxpayers and assure program integrity in the future.

GAO's current work includes statutory responsibilities for TARP under the Emergency Economic Stability Act and the Recovery Act that include bimonthly reports. GAO also plans work on financial market oversight and reform; efforts to ensure the stability of banking, housing, and financial markets; functioning of the mortgage market and disposition of Fannie Mae and Freddie Mac; monitoring services to assist job seekers and low-income families; plans to boost the economy; the world financial system and trade promotion; and state fiscal conditions.

Trend: Changing dynamics of global interdependence and shifts in power

To respond to the challenges and opportunities of global interdependence, GAO proposes to build on past work to inform Congress and policymakers about the complexities of regulating financial institutions and markets in a globally interconnected and competitive world. GAO also plans cross-border work on regulating the safety of medical products, food, and consumer products to help the Congress monitor and oversee regulatory efforts in these areas.

GAO will evaluate the government's efforts to prevent, prepare for, and respond to public health emergencies; improve the U.S. image abroad; promote exports and job creation.

Trend: Advances in science, technology, engineering, and mathematics

The rapid growth of nano-, biomedical, and information technology carries with it both promise and risks. To support the increasing number and sophistication of congressional requests on complex issues, GAO proposes to expand its knowledge and expertise and has already increased staffing and established a Center for Science, Technology, and Engineering.

For 2010 through 2015, GAO's assessments in science and technology will include nanomaterials, climate remediation, counterterrorism, next-generation space systems, and technology-related social and behavioral norms.

Trend: Increasing impact of networks and virtualization

The growing influence of networks and virtualization is a trend newly recognized in GAO's strategic planning. Falling costs, increasing performance, and wider availability of information networks and virtualization are leading to changes in the way information is created and shared. This change affects not only how people work and learn, but also how they think and what they expect from their government.

GAO will assess federal efforts to promote affordable access to telephone and the Internet, management of government telecommunications and interconnected systems, efforts to strengthen the resiliency of critical national assets, networks, and systems, and improve the federal workforce infrastructure.

Trend: Shifting roles in government and governance

The line between government and nongovernmental work is less clear than it once was: private contractors perform support services for government while government takes on additional roles, responsibilities, and even financial stakes in the private sector. Roles have also shifted between state and local government and the federal government and between government and nongovernmental organizations.

GAO will assess the federal government's strategy for managing its reliance on contractors and identify ways to improve acquisition in federal agencies and opportunities to improve the coordination, collaboration, and governance of networks of governmental and nongovernmental organizations. GAO will also focus efforts on such high-risk areas as the U.S. Postal Service's financial condition, oversight of food and drug safety, and cybersecurity efforts.

Trend: Demographic and societal changes confronting the young and old

To meet the challenges of worldwide population growth, migration, and aging, government policymakers will need solid information and analysis. The federal statistical system is a major contributor of such data and analysis, and so GAO will identify gaps in information and advise agencies on increasing the value of their information products.

These trends and related strategic objectives, performance goals, and key efforts will help assure that GAO continues to support Congress' priorities and respond effectively to its members' concerns. In a time of momentous, rapid, and seemingly constant change, this 5-year plan will also help assure that GAO is ready to meet future demands whether from emerging issues or unforeseen events.

**** Jeanette Franzel, Managing Director, Financial Management and Assurance;
Maxine Hattery, Financial Management and Assurance; U.S. Government
Accountability Office**



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AUDITING SECTION / AMERICAN ACCOUNTING ASSOCIATION

Have You Seen...?

Pennie Bagley, Texas Tech University
Albert Nagy, John Carroll University
Gary Peters, University of Arkansas

“Big Five Audits and Accounting Fraud,” by C. Lennox and J. A. Pittman, *Contemporary Accounting Research* (Volume 27, Issue 1): 209-247.

This study examines whether the negative relation between the presence of a Big Five auditor and fraud likelihood changed in the years leading up to the Sarbanes-Oxley Act of 2002 (SOX) and whether the negative relation is explained by Big Five auditors supplying higher quality audits, or by the endogenous effects of screening by auditors and selection by their clients. The authors examine accounting frauds committed by companies between 1981 and 2001. The authors provide evidence that Big Five firms were consistently associated with a lower incidence of accounting fraud and that the finding is robust to controlling for the endogenous effects of screening by audit firms and selection by their clients. The authors also find that the appearance of Big Five audit quality diminution after 1995 actually reflects an increasing propensity for large companies to commit accounting fraud.

“Litigation Reform, Accounting Discretion, and the Cost of Equity,” J. Boone, I. Khurana, and K. Raman, *Journal of Contemporary Accounting and Economics* (Volume 5 Issue 2): 80-94.

This study examines whether the increase in accounting discretion associated with litigation reform is viewed by investors as opportunistic (i.e., as distorting reported earnings) or as improving the ability of reported earnings to reflect economic value. The authors use the context of the 1995 Public Securities Litigation Reform Act to conduct their investigation. They find evidence consistent with the increase in accounting discretion being viewed as opportunistic by investors. The authors assert that the exogenous nature of the 1995 Act suggests that the observed increase (and pricing) of accounting discretion is related to litigation reform rather than some omitted firm-specific operating characteristic.

“Determining Whether There are any Effects of Incentive Compensation and Stock Ownership on Internal Audit Procedures,” by A. Schneider, *International Journal of Auditing* (Volume 14 Issue 1): 101 - 110

This study examines whether internal auditor incentive compensation and stock ownership affect internal auditors' decisions to extend audit procedures when warranted. The study is motivated by the concern that internal auditors may be reluctant to extend audit procedures in a setting that could have a negative impact on the internal auditor's compensation and/or stock value. Using a randomized response technique to elicit responses from internal auditors, the author finds that while internal auditors may be reluctant to extend audit procedures in some situations, neither incentive compensation nor stock ownership affected the audit planning decisions.

“Audit Value and Charitable Organizations,” by K. Kitching, *Journal of Accounting and Public Policy* (Volume 28, Issue 6): 510-524.

The author investigates the propensity of donors to favor charities that use high quality auditors. Consistent with a signaling perspective, the author finds that charities benefit simply from engaging a higher quality auditor. From an information perspective, donors are more sensitive to changes in reported accounting information verified by a high quality auditor. The author also finds positive associations between the propensity of donations and auditor quality, but that the association dissipates with the size of the charity.

“The influence of litigation risk and internal audit source on reliance decisions,” by B. Arel, *Advances in Accounting* (Forthcoming).

This study examines the association between the external auditor’s reliance decisions and the external auditor’s perceived litigation risk and the source of internal audit services. In an experimental study using 89 practicing Big 4 auditors, this study finds that auditors who perceive low litigation risk from placing reliance on the work of internal auditors will rely more on outsourced internal auditors than in-house internal auditors. The results also show that auditors’ reliance decisions are sensitive to the level of account risk consistent with the risk-based approach to the integrated audit encouraged by the PCAOB.

“Time pressure, task complexity, and audit effectiveness,” by A. R. Bowrin and J. King II, *Managerial Auditing Journal* (Volume 25 Issue 2): 160 – 181

This study examines the relationships among time pressure, audit task complexity and audit effectiveness. Using a field experiment, the author documents a negative, interactional relationship among time pressure, complexity, and effectiveness. The authors interpret their findings as a caution against the urge to reduce the time allowed for performing compliance tests, and provide training to improve the detection rate for all type of compliance deviations. The authors also observe that it may not be appropriate for audit planners to assume a uniform time pressure effect across the various tasks involved in an audit.

“The effect of benchmarked performance measures and strategic analysis on auditors’ risk assessments and mental models,” by W. R. Knechel, S. E. Salterio, N. Kochetova-Kozloskic, *Accounting, Organizations and Society* (Volume 35 Issue 3): 316-333.

The study examines the effect of benchmarking of performance measures and strategic analysis, on the risk judgments of auditors carrying out the initial planning of an audit. The authors conduct an experiment with a Balanced Scorecard for organizing and evaluating analytical evidence about the performance of business units within a large client. They find that external benchmarking can cause an auditor to focus on performance measures that are unique to a business unit and disregard performance measures that are common to multiple business units but not benchmarked. However, they also find that a strategic analysis facilitates a more balanced and accurate assessment of the risks across the business units being evaluated due to auditors developing a more complete mental model of a client.

“How Costly Is The Sarbanes Oxley Act? Evidence on the Effects of the Act on Corporate Profitability,” by A. S. Ahmed, M. L. McAnally, S. Rasmussen, and C. D. Weaver, *Journal of Corporate Finance* (Volume 16 Issue 3): 352-369.

This study investigates the net realized costs of SOX by examining its impact on operating profitability. The authors document a decline in cash flows by 1.3% of total assets after SOX. They also note that these costs are higher for smaller firms, for more complex firms, and for firms with lower-growth opportunities. The authors also observe that the net SOX-related costs are not limited to one-time expenses associated with internal-control design and implementation. In aggregate, for the 1428 firms in their sample, the costs amount to about \$19 billion per year and that profitability is lower for up to four years post-SOX.



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AUDITING SECTION / AMERICAN ACCOUNTING ASSOCIATION

Call for Submissions and Volunteers

Seventeenth Annual Midyear Auditing Section Conference Albuquerque, NM

Mark your calendars now for the Seventeenth Annual Midyear Auditing Section Conference that will be held **January 13–15, 2011** at the **Albuquerque Marriott**. A Doctoral Consortium will be held on January 13, and we will also be offering another Excellence in Audit Education workshop as part of the conference. The remainder of the conference will consist of keynote speakers, panel discussions, and concurrent sessions dealing with a wide variety of contemporary topics related to audit, attestation and assurance practices, education, and research. Awards will be given for the **Best Ph.D. Student Paper** submitted to the conference and for the **Best Manuscript** submitted to the conference. While all papers will be considered for the Best Manuscript award, authors must indicate that they would like to be considered for the Best Ph.D. Student Paper award at the time of submission.

You are encouraged to contribute to the program through submissions of auditing, attestation, and assurance research, education research (including instructional cases), and special session proposals. In addition, the Section will rely on your help in planning and conducting the conference and in providing suggestions for session topics, panels, and/or workshops. **Please consider volunteering to participate as a reviewer, discussant, and/or moderator. Details on how to do so will be posted to the Auditing Section website.**

SUBMISSION GUIDELINES

Research papers should follow the style and submission guidelines of *Auditing: A Journal of Practice & Theory*, including the requirement to submit separate electronic files containing the cover page and the paper itself.¹ Instructional cases should be in a format similar to that used in *Issues in Accounting Education*. Submissions are not eligible for consideration if they have been published or accepted for publication, were presented at the 2010 AAA Annual Meeting, or were presented at more than one AAA regional meeting or other academic conference. Papers presented at the Research Forum of the AAA Annual Meeting **are eligible** for consideration. It should be noted that papers accepted for presentation at the 2011 Midyear Auditing Section Conference may also be submitted for presentation at the AAA Annual Meeting scheduled for August 2011.

SUBMISSION DEADLINE

Submissions must be received by **August 31, 2010** to be considered for the program. Early submission is highly encouraged. Any questions should be addressed to Scott Vandervelde (University of South Carolina) or Mike Wilkins (Texas A&M University) through the following email address: MYM2011@moore.sc.edu.

¹Also, please be sure to remove all identification of the authors, including changing the document "Properties" to "anonymous".