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Public Company Accounting Oversight Board

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Report on

2017 Inspection of B F Borgers CPA PC
(Headquartered in Lakewood, Colorado)

Issued by the

Public Company Accounting Oversight Board

November 19, 2018

THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT

PORTIONS OF THE COMPLETE REPORT ARE OMITTED FROM THIS DOCUMENT IN ORDER TO COMPLY WITH SECTIONS 104(g)(2) AND 105(b)(5)(A) OF THE SARBANES-OXLEY ACT OF 2002

PCAOB RELEASE NO. 104-2019-027A
(Includes portions of Part II of the full report that were not included in PCAOB Release No. 104-2019-027)

2017 INSPECTION OF B F BORGERS CPA PC

Preface

In 2017, the Public Company Accounting Oversight Board ("PCAOB" or "the Board") conducted an inspection of the registered public accounting firm B F Borgers CPA PC ("the Firm") pursuant to the Sarbanes-Oxley Act of 2002 ("the Act").

Inspections are designed and performed to provide a basis for assessing the degree of compliance by a firm with applicable requirements related to auditing issuers. For a description of the procedures the Board's inspectors may perform to fulfill this responsibility, see Part I.C of this report (which also contains additional information concerning PCAOB inspections generally). The inspection included reviews of portions of selected issuer audits. These reviews were intended to identify whether deficiencies existed in the reviewed audit work, and whether such deficiencies indicated defects or potential defects in the Firm's system of quality control over audits. In addition, the inspection included a review of policies and procedures related to certain quality control processes of the Firm that could be expected to affect audit quality.

The Board is issuing this report in accordance with the requirements of the Act. The Board is releasing to the public Part I of the report and portions of Part IV of the report. Part IV of the report consists of the Firm's comments, if any, on a draft of the report. If the nonpublic portions of the report discuss criticisms of or potential defects in the Firm's system of quality control, those discussions also could eventually be made public, but only to the extent the Firm fails to address the criticisms to the Board's satisfaction within 12 months of the issuance of the report. Appendix A presents the text of the paragraphs of the auditing standards that are referenced in Part I.A. in relation to the description of auditing deficiencies there.

Note on this report's citations to auditing standards: On March 31, 2015, the PCAOB adopted a reorganization of its auditing standards using a topical structure and a single, integrated numbering system. See *Reorganization of PCAOB Auditing Standards and Related Amendments to PCAOB Standards and Rules*, PCAOB Release No. 2015-002 (Mar. 31, 2015). The reorganization became effective December 31, 2016. Citations in this report reference the reorganized PCAOB auditing standards.

PROFILE OF THE FIRM[1]

Offices	2 (Erie and Lakewood, Colorado)
Ownership structure	Professional corporation
Partners / professional staff[2]	1 / 16
Issuer audit clients	72
Lead partners on issuer audit work[3]	3

[1] The information presented here is as understood by the inspection team, generally as of the outset of the inspection, based on the Firm's self-reporting and the inspection team's review of certain information. Additional information, including additional detail on audit reports issued by the Firm, is available in the Firm's filings with the Board, available at http://pcaobus.org/Registration/rasr/Pages/RASR_Search.aspx.

[2] The number of partners and professional staff is provided here as an indication of the size of the Firm, and does not necessarily represent the number of the Firm's professionals who participate in audits of issuers. The number of partners cited above represents the number of individuals with an ownership interest in the Firm.

[3] The number of lead partners on issuer audit work represents the total number of Firm personnel (not necessarily limited to personnel with an ownership interest) who had primary responsibility for an issuer audit (as defined in AS 1201, *Supervision of the Audit Engagement*) during the twelve-month period preceding the outset of the inspection.

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's inspection staff ("the inspection team") conducted primary procedures for the inspection from October 23, 2017 to November 10, 2017.[4]

A. Review of Audit Engagements

The inspection procedures included reviews of portions of seven issuer audits performed by the Firm. The inspection team identified matters that it considered to be deficiencies in the performance of the work it reviewed.

The descriptions of the deficiencies in Part I.A of this report include, at the end of the description of each deficiency, references to specific paragraphs of the auditing standards that relate to those deficiencies. The text of those paragraphs is set forth in Appendix A to this report. The references in this sub-Part include only the standards that most directly relate to the deficiencies and do not include all standards that apply to the deficiencies. Further, certain broadly applicable aspects of the auditing standards that may be relevant to a deficiency, such as provisions requiring due professional care, including the exercise of professional skepticism; the accumulation of sufficient appropriate audit evidence; and the performance of procedures that address risks, are not included in any references to the auditing standards in this sub-Part, unless the lack of compliance with these standards is the primary reason for the deficiency. These broadly applicable provisions are described in Part I.B of this report.

Certain deficiencies identified were of such significance that it appeared to the inspection team that the Firm, at the time it issued its audit report, had not obtained sufficient appropriate audit evidence to support its opinion that the financial statements were presented fairly, in all material respects, in conformity with the applicable financial reporting framework. In other words, in these audits, the auditor issued an opinion without satisfying its fundamental obligation to obtain reasonable assurance about whether the financial statements were free of material misstatement.

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[4] For this purpose, "primary procedures" include field work, other review of audit work papers, and the evaluation of the Firm's quality control policies and procedures through review of documentation and interviews of Firm personnel. Primary procedures do not include (1) inspection planning, which is performed prior to primary procedures, and (2) inspection follow-up procedures, wrap-up, analysis of results, and the preparation of the inspection report, which extend beyond the primary procedures.

The fact that one or more deficiencies in an audit reach this level of significance does not necessarily indicate that the financial statements are materially misstated. It is often not possible for the inspection team, based only on the information available from the auditor, to reach a conclusion on those points. As indicated below, however, in one instance, the inspection team identified a failure by the Firm to identify and address appropriately a departure from Generally Accepted Accounting Principles ("GAAP") that appeared to the inspection team to be material.

Whether or not associated with a disclosed financial reporting misstatement, an auditor's failure to obtain the reasonable assurance that the auditor is required to obtain is a serious matter. It is a failure to accomplish the essential purpose of the audit, and it means that, based on the audit work performed, the audit opinion should not have been issued.[5]

The audit deficiencies that reached this level of significance are described below–

A.1. Issuer A

(1) the failure to perform sufficient procedures to test the recording of asset purchase transactions (AS 2301.08; AS 2502.03 and .15; AS 2810.30-.31);

(2) the Firm's failure to identify, or to address appropriately, a departure from GAAP that appeared to the inspection team to be material, which related to the omission of certain required disclosures from the financial statements related to the impairment of intangible assets (AS 2810.30-.31);

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[5] Inclusion in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the Firm's attention. Depending upon the circumstances, compliance with PCAOB standards may require the Firm to perform additional audit procedures, or to inform a client of the need for changes to its financial statements or reporting on internal control, or to take steps to prevent reliance on its previously expressed audit opinions. The Board expects that firms will comply with these standards, and an inspection may include a review of the adequacy of a firm's compliance with these requirements, either with respect to previously identified deficiencies or deficiencies identified during that inspection. Failure by a firm to take appropriate actions, or a firm's misrepresentations in responding to an inspection report, about whether it has taken such actions, could be a basis for Board disciplinary sanctions.

(3) the failure to perform sufficient procedures to test the valuation of intangible assets (AS 2501.04; AS 2502.26, .28, and .39);

(4) the failure to perform sufficient procedures to test the occurrence of revenue (AS 1105.10 and .27; AS 2301.13);

(5) the failure to perform sufficient procedures to test the existence of accounts receivable (AS 1105.27; AS 2301.08); and

(6) the failure to perform sufficient procedures to test the occurrence and valuation of issuances of equity-related instruments (AS 2301.08; AS 2502.03 and .15).

A.2. Issuer B

(1) the failure to perform sufficient procedures to evaluate the accounting for consideration received for the issuance of shares of common stock (AS 2301.11; AS 2810.30-.31);

(2) the failure to perform sufficient procedures to evaluate whether goodwill was impaired (AS 2502.26 and .28; AS 2810.30);

(3) the failure to perform sufficient procedures to test the occurrence and valuation of revenue, including the use of sampling with an inadequate sample size developed without consideration of relevant factors (AS 2301.13; AS 2315.19 and .23-.23A);

(4) the failure to perform sufficient procedures to test the valuation of a receivable (AS 2301.11; AS 2501.11);

(5) the failure to perform sufficient procedures to evaluate the issuer's ability to continue as a going concern and the related disclosures (AS 2415.03, .08, and .11); and

(6) the failure to perform sufficient procedures to test the existence and valuation of accounts receivable (AS 2301.08 and .11; AS 2310.34-.35; AS 2501.11).

A.3. Issuer C

(1) the failure to perform sufficient procedures to test the occurrence and valuation of revenue, including the use of sampling with an inadequate sample size developed without consideration of relevant factors (AS 2301.13; AS 2315.19 and .23-.23A; AS 2810.30); and

(2) the failure to perform sufficient procedures to test the valuation of certain assets (AS 2301.11; AS 2501.11).

A.4. Issuer D

(1) the failure to perform sufficient procedures to test revenue (AS 1105.27; AS 2301.08 and .13; AS 2810.30);

(2) the failure to perform procedures to test the issuer's foreign currency cumulative translation adjustment (AS 2810.30-.31); and

(3) the failure to perform sufficient procedures to test the valuation of gains on nonmonetary transactions (AS 2502.03 and .15).

A.5. Issuer E

(1) the failure to perform sufficient procedures to test the occurrence of revenue and the completeness of deferred revenue (AS 1105.27; AS 2301.13); and

(2) the failure to perform sufficient procedures to test the issuances of preferred stock (AS 1105.27; AS 2301.08).

A.6. Issuer F

(1) the failure to perform sufficient procedures to test the occurrence and valuation of revenue, including the use of sampling with an inadequate sample size developed without consideration of relevant factors (AS 2301.13, .16, .18, and .37; AS 2315.19, .23-.23A, and .25-.26); and

(2) the failure to perform sufficient procedures to test the existence and valuation of certain inventory (AS 2301.45; AS 2315.26-.28).

A.7. Issuer G

the failure to perform sufficient procedures to test the valuation of share-based compensation issued to employees and non-employees for services rendered (AS 2502.03 and .15).

B. Auditing Standards

Each deficiency described above could relate to several applicable provisions of the standards that govern the conduct of audits. The paragraphs of the standards that are cited for each deficiency are those paragraphs that most directly relate to the deficiency. The deficiencies also relate, however, to other paragraphs of those standards and to other auditing standards, including those concerning due professional care, responses to risk assessments, and audit evidence.

Many audit deficiencies involve a lack of due professional care. Paragraphs .02, .05, and .06 of AS 1015, *Due Professional Care in the Performance of Work*, require the independent auditor to plan and perform his or her work with due professional care and set forth aspects of that requirement. AS 1015.07-.09 and paragraph .07 of AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*, specify that due professional care requires the exercise of professional skepticism. These standards state that professional skepticism is an attitude that includes a questioning mind and a critical assessment of the appropriateness and sufficiency of audit evidence.

AS 2301.03, .05, and .08 require the auditor to design and implement audit responses that address the risks of material misstatement. Paragraph .04 of AS 1105, *Audit Evidence*, requires the auditor to plan and perform audit procedures to obtain sufficient appropriate audit evidence to provide a reasonable basis for the audit opinion. Sufficiency is the measure of the quantity of audit evidence, and the quantity needed is affected by the risk of material misstatement (in the audit of financial statements) and the quality of the audit evidence obtained. The appropriateness of evidence is measured by its quality; to be appropriate, evidence must be both relevant and reliable in providing support for the related conclusions.

The paragraphs of the standards that are described immediately above are not cited in Part I.A, unless those paragraphs are the most directly related to the relevant deficiency.

B.1. List of Specific Auditing Standards Referenced in Part I.A.

The table below lists the specific auditing standards that are referenced in Part I.A of this report, cross-referenced to the issuer audits for which each standard is cited.

PCAOB Auditing Standards	Issuers
AS 1105, *Audit Evidence*	A, D, and E
AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*	A, B, C, D, E, and F
AS 2310, *The Confirmation Process*	B
AS 2315, *Audit Sampling*	B, C, and F
AS 2415, *Consideration of an Entity's Ability to Continue as a Going Concern*	B
AS 2501, *Auditing Accounting Estimates*	A, B, and C
AS 2502, *Auditing Fair Value Measurements and Disclosures*	A, B, D, and G
AS 2810, *Evaluating Audit Results*	A, B, C, and D

C. Information Concerning PCAOB Inspections that is Generally Applicable to Triennially Inspected Firms

A Board inspection includes a review of certain portions of selected audit work performed by the inspected firm and a review of certain aspects of the firm's quality control system. The inspections are designed to identify deficiencies in audit work and defects or potential defects in the firm's system of quality control related to the firm's audits. The focus on deficiencies, defects, and potential defects necessarily carries through to reports on inspections and, accordingly, Board inspection reports are not intended to serve as balanced report cards or overall rating tools. Further, the inclusion in an inspection report of certain deficiencies, defects, and potential defects should not be construed as an indication that the Board has made any determination about other aspects of the inspected firm's systems, policies, procedures, practices, or conduct not included within the report.

C.1. Reviews of Audit Work

Inspections include reviews of portions of selected audits of financial statements and, where applicable, audits of internal control over financial reporting ("ICFR"). For these audits, the inspection team selects certain portions of the audits for inspection, and it reviews the engagement team's work papers and interviews engagement personnel regarding those portions. If the inspection team identifies a potential issue that it is unable to resolve through discussion with the firm and any review of additional work papers or other documentation, the inspection team ordinarily provides the firm with a written comment form on the matter and the firm is allowed the opportunity to provide a written response to the comment form. If the response does not resolve the inspection team's concerns, the matter is considered a deficiency and is evaluated for inclusion in the inspection report.

The inspection team selects the audits, and the specific portions of those audits, that it will review, and the inspected firm is not allowed an opportunity to limit or influence the selections. Audit deficiencies that the inspection team may identify include a firm's failure to identify, or to address appropriately, financial statement misstatements, including failures to comply with disclosure requirements,[6] as well as a firm's failure to perform, or to perform sufficiently, certain necessary audit procedures. An inspection may not involve the review of all of the firm's audits, nor is it designed to identify every deficiency in the reviewed audits. Accordingly, a Board inspection report should not be understood to provide any assurance that a firm's audit work, or the relevant issuers' financial statements or reporting on ICFR, are free of any deficiencies not specifically described in an inspection report.

In some cases, the conclusion that a firm did not perform a procedure may be based on the absence of documentation and the absence of persuasive other evidence, even if the firm claimed to have performed the procedure. AS 1215, *Audit Documentation*, provides that, in various circumstances including PCAOB inspections, a

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[6] When it comes to the Board's attention that an issuer's financial statements appear not to present fairly, in a material respect, the financial position, results of operations, or cash flows of the issuer in conformity with the applicable financial reporting framework, the Board's practice is to report that information to the Securities and Exchange Commission ("SEC" or "the Commission"), which has jurisdiction to determine proper accounting in issuers' financial statements. Any description in this report of financial statement misstatements or failures to comply with SEC disclosure requirements should not be understood as an indication that the SEC has considered or made any determination regarding these issues unless otherwise expressly stated.

firm that has not adequately documented that it performed a procedure, obtained evidence, or reached an appropriate conclusion must demonstrate with persuasive other evidence that it did so, and that oral assertions and explanations alone do not constitute persuasive other evidence. In reaching its conclusions, an inspection team considers whether audit documentation or other evidence that a firm might provide to the inspection team supports the firm's contention that it performed a procedure, obtained evidence, or reached an appropriate conclusion. In the case of every matter cited in the public portion of a final inspection report, the inspection team has carefully considered any contention by the firm that it did so but just did not document its work, and the inspection team has concluded that the available evidence does not support the contention that the firm sufficiently performed the necessary work.

Identified deficiencies in the audit work that exceed a significance threshold (which is described in Part I.A of the inspection report) are summarized in the public portion of the inspection report.[7]

The Board cautions against extrapolating from the results presented in the public portion of a report to broader conclusions about the frequency of deficiencies throughout the firm's practice. Individual audits and areas of inspection focus are most often selected on a risk-weighted basis and not randomly. Areas of focus vary among selected audits, but often involve audit work on the most difficult or inherently uncertain areas of financial statements. Thus, the audit work is generally selected for inspection based on factors that, in the inspection team's view, heighten the possibility that auditing deficiencies are present, rather than through a process intended to identify a representative sample.

C.2. Review of a Firm's Quality Control System

QC 20, *System of Quality Control for a CPA Firm's Accounting and Auditing Practice*, provides that an auditing firm has a responsibility to ensure that its personnel comply with the applicable professional standards. This standard specifies that a firm's system of quality control should encompass the following elements: (1) independence,

[7] The discussion in this report of any deficiency observed in a particular audit reflects information reported to the Board by the inspection team and does not reflect any determination by the Board as to whether the Firm has engaged in any conduct for which it could be sanctioned through the Board's disciplinary process. In addition, any references in this report to violations or potential violations of law, rules, or professional standards are not a result of an adversarial adjudicative process and do not constitute conclusive findings for purposes of imposing legal liability.

integrity, and objectivity; (2) personnel management; (3) acceptance and continuance of issuer audit engagements; (4) engagement performance; and (5) monitoring.

The inspection team's assessment of a firm's quality control system is derived both from the results of its procedures specifically focused on the firm's quality control policies and procedures, and also from inferences that can be drawn from deficiencies in the performance of individual audits. Audit deficiencies, whether alone or when aggregated, may indicate areas where a firm's system has failed to provide reasonable assurance of quality in the performance of audits. Even deficiencies that do not result in an insufficiently supported audit opinion may indicate a defect or potential defect in a firm's quality control system.[8] If identified deficiencies, when accumulated and evaluated, indicate defects or potential defects in the firm's system of quality control, the nonpublic portion of this report would include a discussion of those issues. When evaluating whether identified deficiencies in individual audits indicate a defect or potential defect in a firm's system of quality control, the inspection team considers the nature, significance, and frequency of deficiencies;[9] related firm methodology, guidance, and practices; and possible root causes.

Inspections also include a review of certain of the firm's practices, policies, and processes related to audit quality, which constitute a part of the firm's quality control system. This review addresses practices, policies, and procedures concerning audit performance, training, compliance with independence standards, client acceptance and retention, and the establishment of policies and procedures.

END OF PART I

[8] Not every audit deficiency suggests a defect or potential defect in a firm's quality control system, and this report may not discuss every audit deficiency the inspection team identified.

[9] An evaluation of the frequency of a type of deficiency may include consideration of how often the inspection team reviewed audit work that presented the opportunity for similar deficiencies to occur. In some cases, even a type of deficiency that is observed infrequently in a particular inspection may, because of some combination of its nature, its significance, and the frequency with which it has been observed in previous inspections of the firm, be cause for concern about a quality control defect or potential defect.

PORTIONS OF THE REST OF THIS REPORT ARE NONPUBLIC AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

PART II

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B. Issues Related to Quality Controls

A firm's system of quality control should provide reasonable assurance of compliance with applicable professional standards and regulatory requirements with respect to its audit practice. (QC 20.04 and .17) On the basis of the information reported by the inspection team, including the audit performance deficiencies described in Part II.A (and summarized in Part I.A) and any other deficiencies identified below, the Board has concerns that the Firm's system of quality control fails to provide such reasonable assurance in at least the following respects[10] –

* * * *

Client Acceptance and Continuance and Personnel Management

The Firm's system of quality control may not provide sufficient assurance that the Firm undertakes only those engagements that it can reasonably expect to complete with professional competence, taking into account the circumstances of competing time demands on the Firm's engagement personnel assigned to lead the audits or assigns work to personnel having the degree of technical training and proficiency required in the circumstances. During the inspection period, one of the Firm's partners served as lead partner on audits for 62 issuers (including 36 with calendar year ends). During the inspection period, another of the Firm's partners served as engagement quality reviewer on audits for 59 issuers (including 33 with calendar year ends). The inspection results provide cause for concern about whether, given the lead partner and engagement quality reviewer's current proficiency and professional competence, the competing time demands of those audits contribute to failures to meet PCAOB standards in the performance of the audit work.

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[10] This report's description of quality control issues is based on the inspection team's observations during the primary inspection procedures. Any changes or improvements that the Firm may have made in its system of quality control since that time may not be reflected in this report, but * * * * [have been] taken into account by the Board during its assessment of whether the Firm has satisfactorily addressed the quality control criticisms or defects within the twelve months after the issuance of this report.

Engagement Quality Review

Questions exist about the effectiveness of the Firm's system of quality control with respect to the execution of engagement quality reviews in compliance with AS 1220, *Engagement Quality Review*. In three of the audits reviewed, the engagement quality reviewer did not possess the level of knowledge and competence related to accounting, * * * *, and financial reporting required to serve as the engagement quality reviewer because of a lack of experience in auditing issuer clients and regulatory reporting. [Issuers A, B, and D]

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PCAOB Standards and Rules

The table below lists the specific PCAOB standards and rules that are primarily related to the descriptions of defects in, or criticisms of, the Firm's system of quality control included in this Part of the report.[11]

PCAOB Standards / Rules
* * * *
AS 1220, *Engagement Quality Review*

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[11] This table does not necessarily include reference to every standard or rule that may have been related to the criticisms or potential defects that are included in Part II.

PART IV

RESPONSE OF THE FIRM TO DRAFT INSPECTION REPORT

Pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(a), the Board provided the Firm an opportunity to review and comment on a draft of this report. The Firm did not provide a written response.

APPENDIX A

AUDITING STANDARDS REFERENCED IN PART I

This appendix provides the text of the auditing standard paragraphs that are referenced in Part I.A of this report. Footnotes that are included in this appendix, and any other Notes, are from the original auditing standards that are referenced. While this appendix contains the specific portions of the relevant standards cited with respect to the deficiencies in Part I.A of this report, other portions of the standards (including those described in Part I.B of this report) may provide additional context, descriptions, related requirements, or explanations; the complete standards are available on the PCAOB's website at http://pcaobus.org/STANDARDS/Pages/default.aspx.[12]

AS 1105, *Audit Evidence*		
SUFFICIENT APPROPRIATE AUDIT EVIDENCE		
Using Information Produced by the Company		
AS 1105.10	When using information produced by the company as audit evidence, the auditor should evaluate whether the information is sufficient and appropriate for purposes of the audit by performing procedures to:[3] ▪ Test the accuracy and completeness of the information, or test the controls over the accuracy and completeness of that information; and ▪ Evaluate whether the information is sufficiently precise and detailed for purposes of the audit.	Issuer A
<u>Footnote to AS 1105.10</u> [3] When using the work of a specialist engaged or employed by management, *see* AS 1210, *Using the Work of a Specialist.* When using information produced by a service organization or a service auditor's report as audit evidence, *see* AS 2601, *Consideration of an Entity's Use of a Service Organization*, and for integrated audits, *see* AS 2201, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.		

[12] The text presented in this appendix represents the standards as in effect during the applicable audit period.

AS 1105, *Audit Evidence*		
SELECTING ITEMS FOR TESTING TO OBTAIN AUDIT EVIDENCE		
Selecting Specific Items		
AS 1105.27	The application of audit procedures to items that are selected as described in paragraphs .25-.26 of this standard does not constitute audit sampling, and the results of those audit procedures cannot be projected to the entire population.[12]	Issuers A, D, and E
Footnote to AS 1105.27 12 If misstatements are identified in the selected items, *see* AS 2810.12 - .13 and AS 2810.17 - .19.		

AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*		
RESPONSES INVOLVING THE NATURE, TIMING, AND EXTENT OF AUDIT PROCEDURES		
AS 2301.08	The auditor should design and perform audit procedures in a manner that addresses the assessed risks of material misstatement for each relevant assertion of each significant account and disclosure.	Issuers A, B, D, and E
Responses to Significant Risks		
AS 2301.11	For significant risks, the auditor should perform substantive procedures, including tests of details, that are specifically responsive to the assessed risks. Note: AS 2110 discusses identification of significant risks[10] and states that fraud risks are significant risks.	Issuers B and C
Footnote to AS 2301.11 10 *See* AS 2110.71 for factors that the auditor should evaluate in determining which risks are significant risks.		

AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*		
Responses to Fraud Risks		
AS 2301.13	*Addressing Fraud Risks in the Audit of Financial Statements*. In the audit of financial statements, the auditor should perform substantive procedures, including tests of details, that are specifically responsive to the assessed fraud risks. If the auditor selects certain controls intended to address the assessed fraud risks for testing in accordance with paragraphs .16-.17 of this standard, the auditor should perform tests of those controls.	Issuers A, B, C, D, E, and F
TESTING CONTROLS		
Testing Controls in an Audit of Financial Statements		
AS 2301.16	*Controls to be Tested.* If the auditor plans to assess control risk at less than the maximum by relying on controls,[12] and the nature, timing, and extent of planned substantive procedures are based on that lower assessment, the auditor must obtain evidence that the controls selected for testing are designed effectively and operated effectively during the entire **period of reliance**.[13] However, the auditor is not required to assess control risk at less than the maximum for *all* relevant assertions and, for a variety of reasons, the auditor may choose not to do so.	Issuer F
Footnote to AS 2301.16 [12] Reliance on controls that is supported by sufficient and appropriate audit evidence allows the auditor to assess control risk at less than the maximum, which results in a lower assessed risk of material misstatement. In turn, this allows the auditor to modify the nature, timing, and extent of planned substantive procedures. [13] Terms defined in Appendix A, *Definitions*, are set in **boldface type** the first time they appear.		
AS 2301.18	*Evidence about the Effectiveness of Controls in the Audit of Financial Statements*. In designing and performing tests of controls for the audit of financial statements, the evidence necessary to support the auditor's control risk assessment depends on the degree of reliance the auditor plans to place on the effectiveness of a control. The auditor should obtain more persuasive audit evidence from tests of controls the greater the reliance the auditor places on the effectiveness of a control. The auditor also should obtain more persuasive evidence about the effectiveness of controls for each	Issuer F

AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*		
	relevant assertion for which the audit approach consists primarily of tests of controls, including situations in which substantive procedures alone cannot provide sufficient appropriate audit evidence.	
SUBSTANTIVE PROCEDURES		
AS 2301.37	As the assessed risk of material misstatement increases, the evidence from substantive procedures that the auditor should obtain also increases. The evidence provided by the auditor's substantive procedures depends upon the mix of the nature, timing, and extent of those procedures. Further, for an individual assertion, different combinations of the nature, timing, and extent of testing might provide sufficient appropriate evidence to respond to the assessed risk of material misstatement.	Issuer F
Timing of Substantive Procedures		
AS 2301.45	When substantive procedures are performed at an interim date, the auditor should cover the remaining period by performing substantive procedures, or substantive procedures combined with tests of controls, that provide a reasonable basis for extending the audit conclusions from the interim date to the period end. Such procedures should include (a) comparing relevant information about the account balance at the interim date with comparable information at the end of the period to identify amounts that appear unusual and investigating such amounts and (b) performing audit procedures to test the remaining period.	Issuer F

AS 2310, *The Confirmation Process*		
CONFIRMATION OF ACCOUNTS RECEIVABLE		
AS 2310.34	For the purpose of this section, *accounts receivable* means— *a.* The entity's claims against customers that have arisen from the sale of goods or services in the normal course of business, and *b.* A financial institution's loans. Confirmation of accounts receivable is a generally accepted auditing procedure. As discussed in paragraph	Issuer B

AS 2310, *The Confirmation Process*		
	.06, it is generally presumed that evidence obtained from third parties will provide the auditor with higher-quality audit evidence than is typically available from within the entity. Thus, there is a presumption that the auditor will request the confirmation of accounts receivable during an audit unless one of the following is true: ▪ Accounts receivable are immaterial to the financial statements. ▪ The use of confirmations would be ineffective.[4] ▪ The auditor's combined assessed level of inherent and control risk is low, and the assessed level, in conjunction with the evidence expected to be provided by analytical procedures or other substantive tests of details, is sufficient to reduce audit risk to an acceptably low level for the applicable financial statement assertions. In many situations, both confirmation of accounts receivable and other substantive tests of details are necessary to reduce audit risk to an acceptably low level for the applicable financial statement assertions.	
Footnote to AS 2310.34 [4] For example, if, based on prior years' audit experience or on experience with similar engagements, the auditor concludes that response rates to properly designed confirmation requests will be inadequate, or if responses are known or expected to be unreliable, the auditor may determine that the use of confirmations would be ineffective.		
AS 2310.35	An auditor who has not requested confirmations in the examination of accounts receivable should document how he or she overcame this presumption.	Issuer B

AS 2315, *Audit Sampling*		
SAMPLING IN SUBSTANTIVE TESTS OF DETAILS		
Planning Samples		
AS 2315.19	After assessing and considering the levels of inherent and control risks, the auditor performs substantive tests to restrict detection risk to an acceptable level. As the assessed levels of inherent risk, control risk, and detection risk for other substantive procedures directed toward the same specific audit objective decreases, the auditor's allowable risk of incorrect acceptance for the substantive tests of details increases and, thus, the smaller the required sample size for the substantive tests of details. For example, if inherent and control risks are assessed at the maximum, and no other substantive tests directed toward the same specific audit objectives are performed, the auditor should allow for a low risk of incorrect acceptance for the substantive tests of details.[3] Thus, the auditor would select a larger sample size for the tests of details than if he allowed a higher risk of incorrect acceptance.	Issuers B, C, and F
Footnote to AS 2315.19 3 Some auditors prefer to think of risk levels in quantitative terms. For example, in the circumstances described, an auditor might think in terms of a 5 percent risk of incorrect acceptance for the substantive test of details. Risk levels used in sampling applications in other fields are not necessarily relevant in determining appropriate levels for applications in auditing because an audit includes many interrelated tests and sources of evidence.		
AS 2315.23	To determine the number of items to be selected in a sample for a particular substantive test of details, the auditor should take into account tolerable misstatement for the population; the allowable risk of incorrect acceptance (based on the assessments of inherent risk, control risk, and the detection risk related to the substantive analytical procedures or other relevant substantive tests); and the characteristics of the population, including the expected size and frequency of misstatements.	Issuers B, C, and F
AS 2315.23A	Table 1 of the Appendix describes the effects of the factors discussed in the preceding paragraph on sample sizes in a statistical or nonstatistical sampling approach. When circumstances are similar, the effect on sample size of those factors should be similar regardless of	Issuers B, C, and F

AS 2315, *Audit Sampling*		
	whether a statistical or nonstatistical approach is used. Thus, when a nonstatistical sampling approach is applied properly, the resulting sample size ordinarily will be comparable to, or larger than, the sample size resulting from an efficient and effectively designed statistical sample.	
Performance and Evaluation		
AS 2315.25	Auditing procedures that are appropriate to the particular audit objective should be applied to each sample item. In some circumstances the auditor may not be able to apply the planned audit procedures to selected sample items because, for example, supporting documentation may be missing. The auditor's treatment of unexamined items will depend on their effect on his evaluation of the sample. If the auditor's evaluation of the sample results would not be altered by considering those unexamined items to be misstated, it is not necessary to examine the items. However, if considering those unexamined items to be misstated would lead to a conclusion that the balance or class contains material misstatement, the auditor should consider alternative procedures that would provide him with sufficient evidence to form a conclusion. The auditor also should evaluate whether the reasons for his or her inability to examine the items have (a) implications in relation to his or her risk assessments (including the assessment of fraud risk), (b) implications regarding the integrity of management or employees, and (c) possible effects on other aspects of the audit.	Issuer F
AS 2315.26	The auditor should project the misstatement results of the sample to the items from which the sample was selected.[5,6] There are several acceptable ways to project misstatements from a sample. For example, an auditor may have selected a sample of every twentieth item (50 items) from a population containing one thousand items. If he discovered overstatements of $3,000 in that sample, the auditor could project a $60,000 overstatement by dividing the amount of misstatement in the sample by the fraction of total items from the population included in the sample. The auditor should add that projection to the misstatements discovered in any items examined 100 percent. This total projected misstatement should be compared with the tolerable misstatement for the account balance or class of transactions, and appropriate consideration should be given to sampling risk. If the total projected misstatement is less than tolerable misstatement for the account balance or class of transactions, the auditor should consider the risk that such a result might be	Issuer F

AS 2315, *Audit Sampling*		
	obtained even though the true monetary misstatement for the population exceeds tolerable misstatement. For example, if the tolerable misstatement in an account balance of $1 million is $50,000 and the total projected misstatement based on an appropriate sample (see paragraph .23) is $10,000, he may be reasonably assured that there is an acceptably low sampling risk that the true monetary misstatement for the population exceeds tolerable misstatement. On the other hand, if the total projected misstatement is close to the tolerable misstatement, the auditor may conclude that there is an unacceptably high risk that the actual misstatements in the population exceed the tolerable misstatement. An auditor uses professional judgment in making such evaluations.	
<u>Footnotes to AS 2315.26</u> 5 If the auditor has separated the items subject to sampling into relatively homogeneous groups (*see* paragraph .22), he separately projects the misstatement results of each group and sums them. 6 AS 2810.10 through .23 discuss the auditor's consideration of differences between the accounting records and the underlying facts and circumstances.		
AS 2315.27	In addition to the evaluation of the frequency and amounts of monetary misstatements, consideration should be given to the qualitative aspects of the misstatements. These include (*a*) the nature and cause of misstatements, such as whether they are differences in principle or in application, are errors or are caused by fraud, or are due to misunderstanding of instructions or to carelessness, and (*b*) the possible relationship of the misstatements to other phases of the audit. The discovery of fraud ordinarily requires a broader consideration of possible implications than does the discovery of an error.	Issuer F
AS 2315.28	If the sample results suggest that the auditor's planning assumptions were incorrect, he should take appropriate action. For example, if monetary misstatements are discovered in a substantive test of details in amounts or frequency that is greater than is consistent with the assessed levels of inherent and control risk, the auditor should alter his risk assessments. The auditor should also consider whether to modify the other audit tests that were designed based upon the inherent and control risk assessments. For example, a large number of misstatements discovered in confirmation of receivables may indicate the need to reconsider the control risk assessment related to the assertions that impacted the design of substantive tests of sales or cash receipts.	Issuer F

AS 2415, *Consideration of an Entity's Ability to Continue as a Going Concern*		
THE AUDITOR'S RESPONSIBILITY		
AS 2415.03	The auditor should evaluate whether there is substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time in the following manner: a. The auditor considers whether the results of his procedures performed in planning, gathering evidential matter relative to the various audit objectives, and completing the audit identify conditions and events that, when considered in the aggregate, indicate there could be substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time. It may be necessary to obtain additional information about such conditions and events, as well as the appropriate evidential matter to support information that mitigates the auditor's doubt. b. If the auditor believes there is substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time, he should (1) obtain information about management's plans that are intended to mitigate the effect of such conditions or events, and (2) assess the likelihood that such plans can be effectively implemented. c. After the auditor has evaluated management's plans, he concludes whether he has substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time. If the auditor concludes there is substantial doubt, he should (1) consider the adequacy of disclosure about the entity's possible inability to continue as a going concern for a reasonable period of time, and (2) include an explanatory paragraph (following the opinion paragraph) in his audit report to reflect his conclusion. If the auditor concludes that substantial doubt does not exist, he should consider the need for disclosure.	Issuer B

CONSIDERATION OF MANAGEMENT'S PLANS		
AS 2415.08	When evaluating management's plans, the auditor should identify those elements that are particularly significant to overcoming the adverse effects of the conditions and events and should plan and perform auditing procedures to obtain evidential matter about them. For example, the auditor should consider the adequacy of support regarding the ability to obtain additional financing or the planned disposal of assets.	Issuer B
CONSIDERATION OF FINANCIAL STATEMENT EFFECTS		
AU 2415.11	When, primarily because of the auditor's consideration of management's plans, he concludes that substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time is alleviated, he should consider the need for disclosure of the principal conditions and events that initially caused him to believe there was substantial doubt. The auditor's consideration of disclosure should include the possible effects of such conditions and events, and any mitigating factors, including management's plans.	Issuer B

AS 2501, *Auditing Accounting Estimates*		
AS 2501.04	The auditor is responsible for evaluating the reasonableness of accounting estimates made by management in the context of the financial statements taken as a whole. As estimates are based on subjective as well as objective factors, it may be difficult for management to establish controls over them. Even when management's estimation process involves competent personnel using relevant and reliable data, there is potential for bias in the subjective factors. Accordingly, when planning and performing procedures to evaluate accounting estimates, the auditor should consider, with an attitude of professional skepticism, both the subjective and objective factors.	Issuer A

AS 2501, *Auditing Accounting Estimates*		
EVALUATING ACCOUNTING ESTIMATES		
Evaluating Reasonableness		
AS 2501.11	Review and test management's process. In many situations, the auditor assesses the reasonableness of an accounting estimate by performing procedures to test the process used by management to make the estimate. The following are procedures the auditor may consider performing when using this approach: d. Identify whether there are controls over the preparation of accounting estimates and supporting data that may be useful in the evaluation. e. Identify the sources of data and factors that management used in forming the assumptions, and consider whether such data and factors are relevant, reliable, and sufficient for the purpose based on information gathered in other audit tests. f. Consider whether there are additional key factors or alternative assumptions about the factors. g. Evaluate whether the assumptions are consistent with each other, the supporting data, relevant historical data, and industry data. h. Analyze historical data used in developing the assumptions to assess whether the data is comparable and consistent with data of the period under audit, and consider whether such data is sufficiently reliable for the purpose. i. Consider whether changes in the business or industry may cause other factors to become significant to the assumptions. j. Review available documentation of the assumptions used in developing the accounting estimates and inquire about any other plans, goals, and objectives of the entity, as well as consider their relationship to the assumptions. k. Consider using the work of a specialist regarding certain assumptions (AS 1210, *Using the Work of a Specialist*). l. Test the calculations used by management to translate the assumptions and key factors into the accounting estimate.	Issuers B and C

AS 2502, *Auditing Fair Value Measurements and Disclosures*		
INTRODUCTION		
AS 2502.03	The auditor should obtain sufficient appropriate audit evidence to provide reasonable assurance that fair value measurements and disclosures are in conformity with GAAP. GAAP requires that certain items be measured at fair value. Financial Accounting Standards Board (FASB) Statement of Financial Accounting Concepts No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements*, defines the fair value of an asset (liability) as "the amount at which that asset (or liability) could be bought (or incurred) or sold (or settled) in a current transaction between willing parties, that is, other than in a forced or liquidation sale."[1] Although GAAP may not prescribe the method for measuring the fair value of an item, it expresses a preference for the use of observable market prices to make that determination. In the absence of observable market prices, GAAP requires fair value to be based on the best information available in the circumstances.	Issuers A, D, and G
Footnote to AS 2502.03 1 Generally accepted accounting principles (GAAP) contain various definitions of fair value. However, all of the definitions reflect the concepts in the definition that appears in Financial Accounting Standards Board (FASB) Statement of Financial Accounting Concepts No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements*. For example, Governmental Accounting Standards Board Statement of Governmental Accounting Standards No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, defines fair value as "the amount at which an investment could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale."		
EVALUATING CONFORMITY OF FAIR VALUE MEASUREMENTS AND DISCLOSURES WITH GAAP		
AS 2502.15	The auditor should evaluate whether the fair value measurements and disclosures in the financial statements are in conformity with GAAP. The auditor's understanding of the requirements of GAAP and knowledge of the business and industry, together with the results of other audit procedures, are used to evaluate the accounting for assets or liabilities requiring fair value measurements, and the disclosures about the basis for the fair value measurements and significant uncertainties related thereto.	Issuers A, D, and G

AS 2502, *Auditing Fair Value Measurements and Disclosures*		
TESTING THE ENTITY'S FAIR VALUE MEASUREMENTS AND DISCLOSURES		
Testing Management's Significant Assumptions, the Valuation Model, and the Underlying Data		
AS 2502.26	The auditor's understanding of the reliability of the process used by management to determine fair value is an important element in support of the resulting amounts and therefore affects the nature, timing, and extent of audit procedures. When testing the entity's fair value measurements and disclosures, the auditor evaluates whether: a. Management's assumptions are reasonable and reflect, or are not inconsistent with, market information (*see* paragraph .06). b. The fair value measurement was determined using an appropriate model, if applicable. c. Management used relevant information that was reasonably available at the time.	Issuers A and B
AS 2502.28	Where applicable, the auditor should evaluate whether the significant assumptions used by management in measuring fair value, taken individually and as a whole, provide a reasonable basis for the fair value measurements and disclosures in the entity's financial statements.	Issuers A and B
AS 2502.39	The auditor should test the data used to develop the fair value measurements and disclosures and evaluate whether the fair value measurements have been properly determined from such data and management's assumptions. Specifically, the auditor evaluates whether the data on which the fair value measurements are based, including the data used in the work of a specialist, is accurate, complete, and relevant; and whether fair value measurements have been properly determined using such data and management's assumptions. The auditor's tests also may include, for example, procedures such as verifying the source of the data, mathematical recomputation of inputs, and reviewing of information for internal consistency, including whether such information is consistent with management's intent and ability to carry out specific courses of action discussed in paragraph .17.	Issuer A

AS 2810, *Evaluating Audit Results*		
EVALUATING THE RESULTS OF THE AUDIT OF FINANCIAL STATEMENTS		
Evaluating the Presentation of the Financial Statements, Including the Disclosures		
AS 2810.30	The auditor must evaluate whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework. Note: AS 2815, *The Meaning of "Present Fairly in Conformity With Generally Accepted Accounting Principles,"* establishes requirements for evaluating the presentation of the financial statements. AS 2820, *Evaluating Consistency of Financial Statements,* establishes requirements regarding evaluating the consistency of the accounting principles used in financial statements. Note: The auditor should look to the requirements of the Securities and Exchange Commission for the company under audit with respect to the accounting principles applicable to that company.	Issuers A, B, C, and D
AS 2810.31	As part of the evaluation of the presentation of the financial statements, the auditor should evaluate whether the financial statements contain the information essential for a fair presentation of the financial statements in conformity with the applicable financial reporting framework. Evaluation of the information disclosed in the financial statements includes consideration of the form, arrangement, and content of the financial statements (including the accompanying notes), encompassing matters such as the terminology used, the amount of detail given, the classification of items in the statements, and the bases of amounts set forth. Note: According to AS 3101 if the financial statements, including the accompanying notes, fail to disclose information that is required by the applicable financial reporting framework, the auditor should express a qualified or adverse opinion and should provide the information in the report, if practicable, unless its omission from the report is recognized as appropriate by a specific auditing standard.[18]	Issuers A, B, and D
<u>Footnote to AS 2810.31</u> [18] AS 3101.41-.44.		