

Report on
2018 Inspection of Michael Trokey & Company, P.C.
(Headquartered in St. Louis, Missouri)

Issued by the
Public Company Accounting Oversight Board
January 2, 2019

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. 104-2019-063

2018 INSPECTION OF MICHAEL TROKEY & COMPANY, P.C.

Preface

In 2018, the Public Company Accounting Oversight Board ("PCAOB" or "the Board") conducted an inspection of the registered public accounting firm Michael Trokey & Company, P.C. ("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 a review of portions of an issuer audit. This review was 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 FIRM¹

Offices	1 (St. Louis, Missouri)
Ownership structure	Professional corporation
Partners / professional staff ²	1 / 1
Issuer audit clients	None at the outset of the inspection; however, the Firm had issued at least one audit report with respect to an issuer since the preceding inspection
Lead partners on issuer audit work ³	1

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 March 26, 2018 to March 30, 2018.⁴

A. Review of Audit Engagement

The inspection procedures included a review of portions of one issuer audit 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 this audit, the auditor issued an opinion without satisfying its fundamental obligation to obtain reasonable assurance about whether the financial statements were free of material misstatement.

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.

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 allowance for loan losses ("ALL") (AS 2301.11; AS 2501.11); and
- (2) the failure to perform sufficient procedures to test the valuation of available-for-sale securities ("AFS securities") (AS 2502.03, .15, and .23).

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 that most directly relate to the deficiency. The deficiencies also relate, however, to other paragraphs of those standards and to other

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.

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 audit for which each standard is cited.

PCAOB Auditing Standards	Issuer
AS 2301, <i>The Auditor's Responses to the Risks of Material Misstatement</i>	A
AS 2501, <i>Auditing Accounting Estimates</i>	A
AS 2502, <i>Auditing Fair Value Measurements and Disclosures</i>	A

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

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

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 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

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.

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.

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, 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.

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

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

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.

PARTS II AND III OF THIS REPORT ARE NONPUBLIC
AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

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 Firm provided a written response to a draft of this report and that response has received careful consideration. Pursuant to section 104(f) of the Act and PCAOB Rule 4007(b), the Firm's response, minus any portion granted confidential treatment, is attached hereto and made part of this final inspection report.¹⁰

¹⁰ The Board does not make public any of a firm's comments that address a nonpublic portion of the report unless a firm specifically requests otherwise. In some cases, the result may be that none of a firm's response is made publicly available. In addition, pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(b), if a firm requests, and the Board grants, confidential treatment for any of the firm's comments on a draft report, the Board does not include those comments in the final report at all. The Board routinely grants confidential treatment, if requested, for any portion of a firm's response that addresses any point in the draft that the Board omits from, or any inaccurate statement in the draft that the Board corrects in, the final report.

MICHAEL TROKEY & COMPANY, P.C.

CERTIFIED PUBLIC ACCOUNTANTS
10411 CLAYTON ROAD
ST. LOUIS, MISSOURI 63131
(314) 432-0996

October 17, 2018

Mr. George Botic
Director of Division of Registration and Inspections
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006

Re: Public Response to Part I of the Draft Inspection Report dated September 17, 2018

Mr. Botic:

PART I

This letter is in response to Part I of the Public Company Accounting Oversight Board ("PCAOB") Draft Inspection Report dated September 17, 2018. While we understand and respect the importance of the inspection function, we must respectfully disagree with the comments.

If possible, we request an exit conference, preferably in person, or by phone, prior to issuance of the final inspection report. We do not feel that the draft comments accurately reflect the quality of the audit work performed and that not all of our audit work performed has been considered.

I considered asking for an "on-site" inspection or to be present at a PCAOB regional office for this inspection. I regret that I did not. While the off-site inspection works well for background information, it makes it extremely difficult to properly communicate and resolve conceptual and technical issues. There are times when we felt that an issue had been clarified and resolved, but the issue was included in the subsequent draft comments. This places small firms at a serious disadvantage. Accounting comment letters received from the Securities and Exchange Commission related to securities filings where we were the auditor of record or consultant over the years have sought clarification of issues. There has been no criticism of material accounting or disclosure issues. Is there a correlation between the quality of the financial statements, including disclosures, and the related audit work?

The Firm believes that the draft inspection report does not reflect the documentation that exists in the work papers. The documentation may be in a different section or form than other firms, but it exists. Where enhanced documentation is necessary we will, of course, change our documentation policy.

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The engagement inspected is a financial institution that is very well-capitalized with relatively simple loan and investment portfolios.

Allowance for Loan Losses ("ALL")

The financial institution has an excellent loan loss history going back many decades. The financial institution does occasionally incur losses on loans. However, ALL exceeded the total of nonperforming loans for the year inspected. Recoveries of loans previous charged-off exceeded charge-offs for the year inspected, although were minimal.

Our Firm has substantial experience working with clients that have loans secured by large real estate projects, including land development, construction, major commercial income-producing projects; non-owner occupied single family loans and residential loans. This financial institution had a clearly defined, low risk level.

Nonetheless, we approached the audit in the same manner as we would have for a financial institution with a more complex environment.

We tested the financial institution's calculation and noted minimal exceptions in historical information, which did not affect the final determination of the adequacy of the ALL balance. Based on that test, along with the results of our audit procedures related to the loan portfolio, we believe that the ALL is well documented. The form of the documentation may be different than other registrants or registered public accounting firms, but the substance is not. It appears that all of our loan documentation has not been fully considered.

Please review our "Allowance for Loan Losses" audit program. That program has been developed and updated based on all relevant resources, including the FASB ASC, Interagency Policy Statements, audit guides, and commercial practice aids. The audit work is done before the program is "signed off" and documentation is located in the work papers.

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Test of Valuation of Available-For-Sale Securities ("AFS")

PCOAB Standards and Related Rules AS 2502.23 indicates, "Because of the wide range of possible fair value measurements, from relatively simple to complex, and the varying levels of risk of material misstatement associated with the process for determining fair values, the auditor's planned audit procedures can vary significantly in nature, timing and extent. For example, substantive tests of the fair value measurements **may** involve (a) testing management's significant assumptions, the valuation model, and the underlying data, (b) developing independent fair value estimates for corroborative purposes, or (c) reviewing subsequent events and transactions" (emphasis added).

PCOAB Standards and Related Rules RB 3101(a)(3) notes that, "The word **"may"** describes actions and procedures that auditors have a responsibility to consider. Matters described in this fashion require the auditor's attention and understanding. How and whether the auditor implements these matters in the audit will depend on the exercise of professional judgment in the circumstances consistent with the objectives of the standard" (emphasis added).

We recognize that there can be differing opinions on professional judgment regarding the tests of fair value on investment securities. However, we believe that the factors below support our compliance with any reasonable interpretation of the standard:

- Very high quality portfolio with full faith and credit of the U.S. Government (MBSs), implied full faith and credit of the U.S. Government (SBA pools) and guarantee of school district bonds by a highly rated state,
- Low and stable interest rate environment at the time of the audit (and expected for the near future based on Federal Reserve Bank minutes),
- Moderate level of interest rate risk (which could affect valuation); mitigated by moderate duration of the portfolio,
- MBSs and SBA pools with recent purchase dates (in a stable interest rate environment).
- The external record keeper obtained the valuation of securities from an independent pricing service under Federal guidelines. The widely held view by the "market" (and the expectation of the Firm) at the time of the audit was that interest rates would remain at historic lows, in a stable rate environment. Because of the high quality of the portfolio, limited duration, low risk profile and economic conditions, our judgment was that this was not an entity risk.

All factors which might affect valuation were considered and deemed to be low risk. Our judgment also indicated that there were other factors (related to AFS securities, e.g. premium amortization on MBSs or unrelated to AFS securities valuation) which carried a higher risk. Further, there were no securities valued using an "issuer model or assumptions".

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We audited all other aspects of the AFS securities, including purchase, premium amortization, test of income, overall test of interest income and confirmation of existence and market value (obtained by a vendor, under Federal guidelines, independent of the registrant and selling broker).

Based on the risk components outlined above and the relatively stable interest rate environment, the risk of a material error in the valuation of AFS was considered remote.

Summary

The Firm is always open to suggestions on how to improve the audit process. We actually modified our documentation policies in certain areas by incorporating suggestions obtained during the inspection process in order to highlight important audit steps performed.

Auditing standards are often general, conceptual and sometimes circular in nature. The audit programs for ALL and AFS securities contain specific procedures to be performed. The actual audit work performed by the Firm and included in the audit work papers support issuance of our opinion of the financial statements.

Based on the facts and circumstances outlined above, the likelihood of a material misstatement of the ALL was assessed as moderate. The likelihood of a material misstatement of the AFS securities was assessed as low. The actual audit work was tailored to the assessment.

We would be most pleased to clarify any unresolved issues.

Very truly yours,

Michael Trokey & Company, P.C.

A handwritten signature in dark ink, appearing to read "Michael Trokey", written in a cursive style.

Michael Trokey, President

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>.¹¹

AS 2301, <i>The Auditor's Responses to the Risks of Material Misstatement</i>		
RESPONSES INVOLVING THE NATURE, TIMING, AND EXTENT OF AUDIT PROCEDURES		
Responses to Significant Risks		
AS 2301.11	<p>For significant risks, the auditor should perform substantive procedures, including tests of details, that are specifically responsive to the assessed risks.</p> <p>Note: AS 2110 discusses identification of significant risks¹⁰ and states that fraud risks are significant risks.</p>	Issuer A
<p><u>Footnote to AS 2301.11</u></p> <p>¹⁰ See AS 2110.71 for factors that the auditor should evaluate in determining which risks are significant risks.</p>		

¹¹ The text presented in this appendix represents the standards as in effect during the applicable audit period.

AS 2501, Auditing Accounting Estimates		
EVALUATING REASONABLENESS		
AS 2501.11	<p>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:</p> <ul style="list-style-type: none"> a. Identify whether there are controls over the preparation of accounting estimates and supporting data that may be useful in the evaluation. b. 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. c. Consider whether there are additional key factors or alternative assumptions about the factors. d. Evaluate whether the assumptions are consistent with each other, the supporting data, relevant historical data, and industry data. e. 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. f. Consider whether changes in the business or industry may cause other factors to become significant to the assumptions. g. 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. h. Consider using the work of a specialist regarding certain assumptions (AS 1210, <i>Using the Work of a Specialist</i>). i. Test the calculations used by management to translate the assumptions and key factors into the accounting estimate. 	Issuer A

AS 2502, Auditing Fair Value Measurements and Disclosure		
INTRODUCTION		
AS 2502.03	<p>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, <i>Using Cash Flow Information and Present Value in Accounting Measurements</i>, 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.</p>	Issuer A
<p><u>Footnote to AS 2502.03</u></p> <p>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, <i>Using Cash Flow Information and Present Value in Accounting Measurements</i>. For example, Governmental Accounting Standards Board Statement of Governmental Accounting Standards No. 31, <i>Accounting and Financial Reporting for Certain Investments and for External Investment Pools</i>, 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."</p>		
EVALUATING CONFORMITY OF FAIR VALUE MEASUREMENTS AND DISCLOSURES WITH GAAP		
AS 2502.15	<p>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.</p>	Issuer A

AS 2502, Auditing Fair Value Measurements and Disclosure		
TESTING THE ENTITY'S FAIR VALUE MEASUREMENTS AND DISCLOSURES		
AS 2502.23	Based on the auditor's assessment of the risk of material misstatement, the auditor should test the entity's fair value measurements and disclosures. Because of the wide range of possible fair value measurements, from relatively simple to complex, and the varying levels of risk of material misstatement associated with the process for determining fair values, the auditor's planned audit procedures can vary significantly in nature, timing, and extent. For example, substantive tests of the fair value measurements may involve (a) testing management's significant assumptions, the valuation model, and the underlying data (see paragraphs .26 through .39), (b) developing independent fair value estimates for corroborative purposes (see paragraph .40), or (c) reviewing subsequent events and transactions (see paragraphs .41 and .42).	Issuer A