

REVIEW OF AMG’S QUARTERLY FINANCIAL STATEMENTS: A SHORT CASE ABOUT AUDITOR RESPONSIBILITIES AND REQUIREMENTS

Kathleen A Simione, Quinnipiac University
Aamer Sheikh, Quinnipiac University

CASE DESCRIPTION

The primary subject matter of this case concerns reviews of interim (quarterly) financial statements. More specifically, this instructional case provides students with a real world example of a failure in the review of interim financial information of a registrant client. The case has a difficulty level of four or five and is appropriate for a senior level or a graduate auditing course either online or on-ground and on an individual or team basis. The case can be completed concurrently with the coverage of other assurance services, specifically, the review of interim financial information for public companies. The case is designed to be taught in a single class period and is expected to require two hours of outside preparation by students.

CASE SYNOPSIS

Review engagements are included in the services that auditors or assurance practitioners provide and are therefore an important topic that should be covered in an auditing course. In addition, standards and requirements for reviews differ from audits, consequently students should have the opportunity to determine the requirements and make decisions relevant to a review of financial statements. This case, based in part upon a Securities and Exchange Commission’s Accounting and Auditing Enforcement Release, requires students to put themselves in the position of the accountant conducting a review of the quarterly financial statements of AMG, a manufacturer of a wide variety of products whose stock trades on an organized exchange. Students have to decide how best to conduct the review given the circumstances, and determine what type of review report, if any, to issue following the relevant Public Company Accounting Oversight Board (PCAOB) standards. The discussion questions are designed to facilitate classroom discussion; however, they can also be used as written homework assignments if classroom time is limited or as online discussion questions in an online class.

INTRODUCTION

In this case, you are placed in the position of the accountant conducting a review of the quarterly financial statements of AMG, a manufacturer headquartered in Dallas, Texas. AMG’s common stock is registered with the Securities and Exchange Commission (SEC) and trades on an organized exchange. Your firm has charged you with deciding how best to conduct this review, and what type of review report, if any, to issue following the relevant Public Company Accounting Oversight Board (PCAOB) standards on reviews of interim financial information.

BACKGROUND

You graduated with your Master's degree in Accountancy from a small private university recently, and went to work immediately for a small (four individual – one Partner, one Manager, and two staff members including yourself) public accounting firm in Dallas, Texas. Earlier this year, you passed your last part of the Certified Public Accountant (CPA) examination, and recently became registered as a CPA in the state of Texas (i.e., licensed with the Texas State Board of Public Accountancy). You worked on your first audits last year for two small privately held clients. In February of this year, you completed your first audit of AMG, your firm's first registrant (publicly traded) client. Your firm issued an unmodified opinion based on the results of your audit work. Auditing a registrant turned out to be more work than you were anticipating, but you learned during the process.

REVIEW OF INTERIM FINANCIAL STATEMENTS

Now, AMG has asked your firm to review their interim (quarterly) financial statements in accordance with the applicable PCAOB professional standards. Your firm agrees to perform such a review. An interim review engagement letter, as required by PCAOB, is signed by your firm and by AMG's audit committee (a committee of AMG's board of directors).

The Partner asks you to begin your review of AMG's interim (quarterly) financial statements. During your review procedures, you discover that during the first quarter of the fiscal year (hereafter abbreviated as Q1), AMG recorded significant amounts of sales near the end of the quarter. Each of these sales was for amounts that were substantially higher than those typically recorded by AMG. For instance, if the average sale during Q1 was for \$5,000, then the average sale recorded near the end of Q1 was for \$100,000. These substantial and material sales were included in the quarter end aging of receivables reports provided to you by the client.

When your firm asked for supporting documentation for these sales near the end of Q1, the client provided your firm with copies of the sales invoices only. This raised your suspicions. You then personally asked the client for any other documentation that might be available related to these substantial quarter end Q1 sales. You were told that the accounting manager had been asked to check if any additional documentation was available but that it might take a few days to find any such documentation. You began to get a sinking feeling that not all might be right with these sales recorded by your client.

You decide to meet in person with AMG's accounting manager. At your meeting with him, you ask about these substantial sales recorded at the end of Q1. He explains that he had been too busy to send invoices to individual customers during the quarter, and thus had "caught up" at the end of the quarter by combining numerous individual sales invoices into a "few larger" sales invoices. He also said that this was the primary reason it was taking him some time to find the additional supporting documentation regarding these substantial sales but that he expected to find all the missing documentation within a few days, and send it to you.

You leave the accounting manager's office disturbed and puzzled about what might be going on. You wonder if your firm that should have accepted this review engagement in the first place, and decide to go back to the office and consult the PCAOB's standards on reviews of interim financial statements, and then to talk to the Partner about how best to proceed.

DISCLAIMER: This case is written using publicly available information to provide a setting for student learning. It is not intended to provide commentary on or evaluation of the effectiveness or appropriateness of any

party's handling of the situation described. Certain names and other information have been changed in order to highlight certain issues and in order to maintain confidentiality and privacy.