

Appendix 11B Problems

Required:

LO 11-4, 6

11B-1. In Part III (Appendix 11B) of the audit case, the audit staff of Adams, Barnes & Co. identified specific revenue risks on working paper RA-12 (page 494). However, the "Summary of Audit Approach" section is incomplete (in process) for risks 2 and 3.

Review the audit program (working paper B-6) on pages 495–496 and identify the substantive audit procedures that were designed specifically to address these risks of material misstatement.

11B-2. Assume that you have been assigned to the audit of Keystone after audit planning has occurred. Review the planning information on pages 235–242 and the audit program for the accounts receivable and revenue (B-6 on pages 495–496). The manager on the engagement has given you the task of reviewing the monthly revenue report on page 498 (B-11).

a. Based on your review of the report, describe any unusual relationships that might indicate a risk of misstatement of revenues based on your knowledge of the company derived from a review of the information on pages 235–242.

b. Identify any procedures on the audit program for receivables and revenue that might address the risk(s) identified in (a).

c. Design two other procedures that would address the risk(s) identified in (a).

11B-3. Keystone Computers & Networks, Inc. (KCN), has 933 accounts receivable, with a total book value of \$10,235,457. From that population, Adams, Barnes & Co. (ABC), CPAs, selected a sample of 260 accounts (142 unique accounts) for confirmation for the year ended December 31, 20X5, as illustrated by the working paper on page 495. First and second confirmation requests resulted in replies for all but 10 of those accounts. ABC performed alternative procedures on those 10 accounts and noted no exceptions. Of the replies, five had exceptions as described below (with ABC follow-up):

1. "The balance of \$120,000 is incorrect because we paid that amount in full on December 31, 20X5." *Follow-up: An analysis of the cash receipts journal revealed that the check had been received in the mail on January 9, 20X6.*

2. "Of the balance of \$30,000, \$330 is incorrect because on December 19 we returned a printer to Keystone when we found that we didn't need it. We ordered it in the middle of November when we had anticipated a need for it. When we received the printer, we realized it was unnecessary and returned it unopened." *Follow-up: An analysis of the transaction revealed that it was received by Keystone on December 31, 20X5, and that the adjustment to the account had been processed on January 2, 20X6.*

3. "The balance of \$214,000 is correct, and we paid it on January 5, 19X6." *Follow-up: An analysis of the cash receipts journal revealed that the check had been received on January 10, 20X6.*

4. "Of the balance of \$130,000, \$10,000 is incorrect because it represents goods that we didn't receive until January 5, 20X6." *Follow-up: Inspection of shipping records reveals that the item was shipped on January 3, 20X6.*

5. "Of the account's \$18,000 balance, we paid \$17,460 and the \$540 (3 percent of the total) remains unpaid because the Keystone salesperson told us that she would be able to obtain a 'special' discount beyond the normal." *Follow-up: While inspection of the sales agreement indicated no such discount arrangement, discussions with Loren Steele (controller) and Sam Best (president) indicated that the salesperson had inappropriately granted such a discount to the client. On January 15 of 20X6, they processed the discount and credited the account for \$540.*

Required:

a. For each of the five exceptions, determine the account's proper "audited value."

b. Use the probability-proportional-to-size method with your analysis from part (a) to evaluate your sample's results. The risk of incorrect acceptance is 5 percent.