



# Rotman Commerce UNIVERSITY OF TORONTO

## Course Outline

### RSM 423 H1 S

Auditing II (Advanced Auditing)

Winter 2017

Course Meets: Tuesdays 4-6 pm in WO 30 (section L0101); Thursdays 4-6 pm in WO 25 (section L0201)

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*(Please include "RSM423" at the beginning of the email subject line)*

**(Note: the above is my preferred email address. Try not to post emails through Blackboard (henceforth Bb) as I check those irregularly.)**

### Course Scope and Mission

This course covers the more advanced assurance sections of the CPA Canada Handbook (henceforth, HB) and related underlying concepts. In addition to covering the technical material in the HB, we will be reviewing some research and controversies of current practice. We consider a range of issues that are important in audit practice. Audit II builds on your introductory course by providing a more thorough coverage of the audit reasoning process, professional judgment and the relationship between auditing and accounting.

### Course Prerequisites

RSM 323

## Course Website

### Logging in to your Blackboard Course Website

Like many other courses, RSM 423 uses Blackboard (Bb) for its course website. To access the RSM 423 website, or any other Blackboard-based course website, go to the UofT portal login page at <http://portal.utoronto.ca> and log in using your UTORid and password. Once you have logged in to the portal using your UTORid and password, look for the **My Courses** module, where you'll find the link to the RSM 423 course website along with the link to all your other Blackboard-based courses.

### Activating your UTORid and Password

If you need information on how to activate your UTORid and set your password for the first time, please go to [www.utorid.utoronto.ca](http://www.utorid.utoronto.ca). Under the "First Time Users" area, click on "activate your UTORid" (if you are new to the university) or "create your UTORid" (if you are a returning student), then follow the instructions. New students who use the link to "activate your UTORid" will find reference to a "Secret Activation Key". This was originally issued to you when you picked up your Tcard at the library. If you have lost your Secret Activation Key you can call 416-978-HELP or visit the Help Desk at the Information Commons on the ground floor of Robarts Library to be issued a new one. **The course instructor will not be able to help you with this.** 416-978-HELP and the Help Desk at the Information Commons can also answer any other questions you may have about your UTORid and password.

### Email

At times, the course instructor may decide to communicate important course information by email. As such, all UofT students are required to have a valid UTmail + email address. You are responsible for ensuring that your UTmail + email address is set up AND properly entered on the ROSI system. For more information please visit <http://help.ic.utoronto.ca/category/3/utmail.html>

Forwarding your utoronto.ca email to a Hotmail, Gmail, Yahoo or other type of email account is not advisable. In some cases, messages from utoronto.ca addresses sent to Hotmail, Gmail or Yahoo accounts are filtered as junk mail, which means that important messages from your course instructor may end up in your spam or junk mail folder.

### Course Material

The course material has been classified into two types:

#### Required and Optional Materials

**Required** materials are necessary to pass the course. This document lists only the required readings that you must know for exams. The required material consists primarily of lecture notes, course slides, and textbook chapter material from Smieliauskas/Bewley.

**All materials should be available on Blackboard (henceforth, Bb) or by clicking on the links in the course outline below (in its electronic form on Bb under course documents), except as noted by \*\*\*.**

**Important Notice.** The exams will cover the course material in the following priority:

1. Class coverage of material (make sure you take good notes),
2. Class lecture notes and complementary power point slides posted on Bb are intended to supply most of the class coverage. These include summaries of required and optional readings, illustrations, and solutions to questions/cases covered in class. The lecture notes do not cover discussions in class that may deviate from the posted material. This is why you are required to take good notes,
3. Other required readings, and
4. Background (optional) readings for those interested.

### **Required Readings**

- 1.\*\*\* Selected chapters from [Auditing, An International Approach](#), McGraw Hill Ryerson, 2016 (7<sup>th</sup> Ed), henceforth SB (or earlier editions, by W. Smieliauskas and K. Bewley)-- or other appropriate text as discussed in class. Don't buy any new textbooks until you have attended the first class!
2. Readings and cases as indicated in class materials of this outline. See below. The readings will be available on Bb as explained below. These readings consist primarily of lecture notes, slides, and selected SB chapters.
3. The CPA Canada Handbook, including the Canadian Audit Standards (CASs), is accessible online at [www.rotman.utoronto.ca/bic/](http://www.rotman.utoronto.ca/bic/) and selecting the "[CPA Canada Standards and Guidance](#)" data base. If you have difficulties with the links, you can contact BIC at [bicstaff@rotman.utoronto.ca](mailto:bicstaff@rotman.utoronto.ca). You should learn to navigate through the CPA Canada Handbook on your own!

**Optional Readings:** Additional readings giving more details on issues discussed in class but not necessary to do well in the course.

## Evaluation and Grades

Grades are a measure of the performance of a student in individual courses. Each student shall be judged on the basis of how well he or she has command of the course materials.

Total allocation of marks is as follows:

Assignments	25%
Midterm (1 hour) – Fri Feb. 10 (at 8-9 am, location to be determined)	25%
Final exam (2 hrs.)	<u>50%</u>
Final mark	<u>100%</u>

There are two assignments both to be done in groups of one to four students. Both assignments are cases that will be made available on the (Bb) site. Further information will be given in class.

+ up to 3 bonus marks for participation in optional 10-15 minute presentations on selected topics to be given by student groups in class. An alternative bonus mark project is to prepare a critical thinking analysis of the IASB (2015) Exposure Draft on the conceptual framework for financial reporting. The May 2015 Exposure Draft on the Conceptual Framework can be found at the following link:

[http://www.ifrs.org/Current-Projects/IASB-Projects/Conceptual-Framework/Documents/May%202015/ED\\_CF\\_MAY%202015.pdf](http://www.ifrs.org/Current-Projects/IASB-Projects/Conceptual-Framework/Documents/May%202015/ED_CF_MAY%202015.pdf)

The written report on your analysis of the discussion paper is due in last class—class 12. Details to be discussed in class. Note that the max bonus marks possible for any student is 3, with no student able to obtain a final mark greater than 100%.

## Course Objectives

1. To develop critical thinking skills for professional judgment in assurance engagements, particularly the audit of accounting estimates and appropriate application of accounting standards under uncertainty,
2. To develop a better understanding of the basic concepts and reasoning underlying accounting and auditing principles, and their integration,
3. To become better acquainted with current issues, research and controversies facing the auditing profession,
4. To obtain advanced technical knowledge of the CPA Canada Handbook—Assurance, and its application, and
5. To obtain an understanding of basic statistical concepts useful to auditors and how this can be extended to help guide broader professional judgment.

## POLICY AND PROCEDURE

### **Missed Tests and Assignments (including midterm examinations)**

Students who miss a test or assignment for reasons entirely beyond their control (e.g. illness) may submit a request for special consideration. Provided that notification and documentation are provided in a timely manner, and that the request is subsequently approved, no academic penalty will be applied.

In such cases, students must notify Rotman Commerce on the date of the missed test (or due date in the case of course work) and submit supporting documentation (e.g. [Verification of Student Illness or Injury form](#)) to the Rotman Commerce Program Office within **48 hours** of the originally scheduled test or due date. Students who do not provide Rotman Commerce or the instructor with appropriate or sufficient supporting documentation will be given a grade of 0 (zero) for the missed test or course deliverable.

**Note that the physician's report must establish that the patient was examined and diagnosed at the time of illness, not after the fact. Rotman Commerce will not accept a statement that merely confirms a report of illness made by the student and documented by the physician.**

**Submission of Assignments** - Late assignments will also be given a mark of zero. A missed midterm will be made up by assigning your final exam mark to the midterm mark. You should talk to your instructor in this or any other course if you are having difficulties with the course work.

**Student Wellness:** You should become familiar with assistance that is available at Commerce office for career and networking advice; and at University Health Services for health, family, relationship, stress, and other personal wellness issues. As the saying goes "an ounce of prevention is worth a pound of cure" so take this into account if you are experiencing or foresee difficulties. The University of Toronto Health and Wellness services are available to all students on the 2<sup>nd</sup> floor of the Koffler Center at 214 College street (416-978-8030) website: <https://www.studentlife.utoronto.ca/hwc/where-did-caps-go>

### **Accessibility Needs**

The University of Toronto is committed to accessibility. If you require accommodations for a disability, or have any accessibility concerns about the course, the classroom or course materials, please contact Accessibility Services as soon as possible: [accessibility.services@utoronto.ca](mailto:accessibility.services@utoronto.ca) or <http://www.accessibility.utoronto.ca/>.

### **Academic Integrity**

Academic Integrity is a fundamental value essential to the pursuit of learning and scholarships at the University of Toronto. Participating honestly, respectfully, responsibly, and fairly in this academic community ensures that the UofT degree that you earn will continue to be valued and respected as a true signifier of a student's individual work and academic achievement. As a result, the University treats cases of academic misconduct very seriously.

*The University of Toronto's Code of Behaviour on Academic Matters*

<http://www.governingcouncil.utoronto.ca/policies/behaveac.htm> outlines the behaviours that constitute academic misconduct, the process for addressing academic offences, and the penalties that may be imposed. You are expected to be familiar with the contents of this document. Potential offences include, but are not limited to:



In papers and assignments:

- Using someone else's ideas or words without appropriate acknowledgement,
- Submitting your own work in more than one course without the permission of the instructor,
- Making up sources or facts, and/or
- Obtaining or providing unauthorized assistance on any assignment (this includes collaborating with others on assignments that are supposed to be completed individually).

On test and exams:

- Using or possessing any unauthorized aid, including a cell phone,
- Looking at someone else's answers,
- Misrepresenting your identity, and/or
- Submitting an altered test for re-grading.

Misrepresentation:

- Falsifying institutional documents or grades, and/or
- Falsifying or altering any documentation required by the University, including (but not limited to), medical notes.

All suspected cases of academic dishonesty will be investigated by the following procedures outlined in the *Code of Behaviour on Academic Matters*. If you have any question about what is or not is permitted in the course, please do not hesitate to contact the course instructor. If you have any questions about appropriate research and citation methods, you are expected to seek out additional information from the instructor or other UofT resources such as College Writing Centres or the Academic Success Centre.

## Weekly Schedule

### Class 1-2: Statistical Auditing: The Foundation of the Audit Risk Concept and Audit Reasoning

#### **Required Readings (click on the link if given, or look for file in Bb):**

- CAS, 500, 530, and AuG-41 (an old CICA Handbook guideline available on Bb that best illustrates how audit standards, until recently, have ignored important uncertainties)
- Lecture notes class 1-2 (posted in Bb)
- Review problem DC 10-4 page 425 SB (same as first class handout).
- Hall, T.W., T.L. Herron, and B.J. Pierce. "[How Reliable is Haphazard Sampling](#)". *CPA Journal*. Jan. 2006: 26-27.
- Giant Store's Case—the power of statistical reasoning to guide audit judgment—posted in Bb.
- The dozy watchdogs; Accounting Scandals:  
<http://search.proquest.com.myaccess.library.utoronto.ca/docview/1636202791/fulltext/10CAA509EADB45FDPQ/16?accountid=14771>
- [Public Report on Big 4 Inspections, Nov. 2016. CPAB](#)

#### **Optional Readings (click on the link or in Bb):**

Gray, G, L, J. L. Turner, P. J. Coram, and T. J. Mock. (2011). Perceptions and Misperceptions Regarding the Unqualified Auditor's Report by Financial Statement Preparers, Users, and Auditors. *Accounting Horizons*. 25(4): 659-684. Comment : This reading is an interesting review of the misconceptions by auditors and users of financial statements on the purpose of audits.

Tucker, J.J. III. 1989.. Development of the Audit Risk Model. *Accounting Horizons*. June (p.28), Comment: If you want to know the logic behind the audit risk model, then this article in Bb should help you understand it better.

The link below gives access to a Forbes study on changing expectations of the auditor's role.

[http://images.forbes.com/forbesinsights/StudyPDFs/Insights\\_GPPC\\_REPORT.pdf](http://images.forbes.com/forbesinsights/StudyPDFs/Insights_GPPC_REPORT.pdf)

### Class 3: Professional Judgment and Skepticism, Audit Reasoning Process and related Basic Reasoning Concepts: and Reliance on Experts.

#### **What is Implied by an Acceptable Reporting Framework?**

#### **Required Readings:**

- Skim CAS 200, 210, 230, 610, 620, 800, Sections 5049 and 5050 (part of new CSAE 3000 as of 2017); AuG 46 (goes with CAS 230).
- Lecture notes class 3 (posted in Bb)
- SB Appendix 3A (same as the one posted on Bb)
- Skim CAS 230, focus especially on A10. See question and solution in section V of the lecture notes for an illustration of how language and choice of words can affect auditor judgment in practice.
- Verreault, D. A., S. Yang, J. Angel. 2004. "[Sprint Corporation: Ethical Decisions and Tax Avoidance Strategies](#)". *Issues in Accounting Education*. Vol.19 No. 1 (February): 119-143.



**Optional Readings (these are summarized in the lecture notes):**

- P. Cowperthwaite. **Tougher than you think.** *CAMagazine*. March 2013: 43-45.
- P. Cowperthwaite. **Good Judgments.** *CAMagazine*. April 2013: 45-47.
- S. Salterio. **Shedding light on negotiations.** *CAMagazine*. April 2013: 54-57
- J Lauck **The Psychology Behind Good Judgment.** *Journal of Accountancy* June 2016:26-30..

**Class 4: Review of Intro Auditing, the Canadian Auditing Standards (CASs) specialized audit topics, introduction to review and compilation engagements, assurance and association frameworks.**

**Required Readings:**

- Skim CPA Canada Handbook Sections 5020, 5021, 5025, 530, 5800, 7050, 7500
- 7600, 8100, 8500, 8600, 9100, 9200, CSAE 3416, 3410, CAS 330, 402, 450, 500, 501, 505, 510, 520, 710, 805, 810
- Lecture notes for class 4
- Ch. 16 SB, pp. 626-640 and 651-657 (or equivalent).
- Special Reports: service organizations: pages 26-28 of chapter 16 old edition posted in Bb for this class.
- Ch. 5-8 SB (review of intro auditing).
- Review problems SB Chapter 6, Question DC 6-1, page 297, Chapter 17, EP 17-2 in Cpnnect SB and three questions in back of lecture notes.. All of these have solutions posted in the lecture notes in Bb.. .
- Hermanson, D.R. "[How Consulting Services Could Kill Private-Sector Auditing.](#)" *CPA Journal*. Jan. 2009: 6-9.

**Class 5: The New Audit Report, Risk-Based Auditing, and Going Concern, and Materiality--the Basic Concepts**

**\*\*\*Mid-term Exam—1 hour test (25 marks) on Friday Feb. 10 , 8-9 am - location TBA. The mid-term test covers the 1<sup>st</sup> 5 weeks of course material.\*\*\***

**Required Readings:**

- Skim through CAS 230, 300, 315, 320, 330, 450, 550, 560, 600, 700, 705, 706.
- Lecture notes for class 5, especially the class problems related to new CASs.
- Also, you can check pages 40-41 (Exhibit 2-2) SB for CAS 700 report.
- Review Chapter 6 SB (same as the ch. 6 posted in Bb)
- New ISA Audit Report starting Dec. 15, 2016 (in Bb)
- CPAB 2014 Conference report (in Bb)
- Summaries of optional readings.

**Class 6: Introduction to Risk Based Reasoning in Financial Reporting (RBR) Principles (also referred to as EBAT)**

**\*\*\*Assignment 1 due in class 6: Case 1 assignment from Assignments folder in Bb**

**Required Reading:**

- CAS 540 and 570.
- Batten et al. 2013: reading on problems auditors are having in verifying accounting estimates and fair values (posted in Bb)
- Makridakis, S., R.M. Hogarth, and A. Gaga. "Why Forecasts Fail. What to Do Instead." MIT Sloan Management Review. Winter 2010. Vo. 51, No. 2: 83-90. (in Bb)
- "opinion shopping" standard on pages 121-122 SB (HB 7600).
- Chapter 19 SB , Part I

**Class 7-8: Assessing the Estimation Uncertainties in Accounting Estimates: Audit Risk vs. Accounting Risk vs. Info Risk vs. Business Risk; FOFI; Ethical Reporting and Risk; Audit Quality and Accounting Quality**

**Required Readings:**

- CAS 540, and 570 (again).
- AuG-41 (again!)
- HB Sections 7150, 7200, 4250 (accounting section of HB), AuG-6, Aug-16
- Cockburn, D. (1992). "At home on the range" CA Magazine. CICA. May: 38-39.
- Lecture Notes class 7-8.
- Chapter 19 SB, Part II (in Bb).
- HB Accounting/Part I-IFRS/2014 edition/The conceptual framework for financial reporting, including measurement uncertainties, IAS 18 (revenues), IAS 37 (contingencies), and IAS (leases).

**Bonus presentation project in class 8: Project 1 consists of summarizing the ongoing Livent litigation. Project 2 consists of appraising the class of business, accounting and audit risks from Alibaba's listing in the New York stock exchange in 2014.**

**Classes 9-10: Corporate Governance; Responsibilities for Detecting Fraud, Illegal Acts, Misleading Reporting, and guidance on helping decide if misstatements are intentional**

**Required Readings:**

- CAS 240 and CAS 250, 260, 265, Sections 5815 and 9110; CSAE 3416, 3410.
- Guidance on Criteria of Control (CPA Canada).
- Investigative and Forensic Accounting (CPA Canada).
- Lecture notes class 9-10.
- Appendix 6B, Chapter 7 including appendixes 7A and 7B, Chapter 21 Part II, and appendix 21A of SB, with focus on application case in Chapter 21.
- Krugman, P. (Nobel Prize in economics 2008). "[Real Bonuses Based on Fake Profits: The Madoff Economy](#)" also in pages 759-760 of SB.
- Benson, S. "[Recognizing the Red Flags of a Ponzi Scheme.](#)" *CPA Journal*. June 2009: 18-25.

**Optional Readings (summarized in lecture notes):**

Dorminey, J., S. Fleming, M. Kronacher, and R.A. Riley Jr. 2012. "The Evolution of Fraud Theory" *Issues in Accounting Education*, Vo. 27 No. 2: 555-579.

## **Class 11: Public Sector Auditing, Assurance on Solvency, Prospectuses**

### **Required Readings:**

- Lecture notes class 11
- Chapters 21 Part I SB
- Skim CAS 720, AuG-4, PS 5000, 5300, 5400, 6410, 6420, CSAE 3001
- MD&A Guidance CPA Canada
- Old ch. 16 in Bb on service auditor reports

## **Class 12: Assignment 2 due in last class; Review of HB 5925: Audit of Internal Control; and review of the course: Audit Quality, Accounting Quality, and Ethical Reporting**

### **Required Readings:**

- Ch. 17 SB pp, 908-912
- Skim HB 5925

**Bonus project 3: class presentation on the potential financial statement effects of accounting risks for Canada's oil companies in light of recent volatility in oil prices. Special software and optional training in data analytics might be available for those wishing to undertake this project.**

**Written report bonus projects due in class 12: A max of 3 bonus marks for the entire course is available for any student.** If you do not get a chance to do a bonus presentation, the alternative bonus mark project is to prepare a report involving a critical analysis from the audit perspective of the IASB's May 28, 2015 Exposure Draft on the Conceptual Framework of Financial Reporting. The Exposure Draft can be found at the following link:

You might also find the basis of conclusions useful in your critical analysis at the following link:

[http://www.ifrs.org/Current-Projects/IASB-Projects/Conceptual-Framework/Documents/May%202015/Basis-to-ED\\_CF\\_MAY%202015.pdf](http://www.ifrs.org/Current-Projects/IASB-Projects/Conceptual-Framework/Documents/May%202015/Basis-to-ED_CF_MAY%202015.pdf)

**Another optional reading will be made available in Bb: MISLEADING FORECASTS IN ACCOUNTING ESTIMATES: A FORM OF ETHICAL BLINDNESS IN ACCOUNTING STANDARDS?**