

Report on

2014 Inspection of Mark Shelley CPA
(Headquartered in Mesa, Arizona)

Issued by the

Public Company Accounting Oversight Board

February 26, 2015

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**

2014 INSPECTION OF MARK SHELLEY CPA

Preface

In 2014, the Public Company Accounting Oversight Board ("PCAOB" or "the Board") conducted an inspection of the registered public accounting firm Mark Shelley CPA ("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). Overall, the inspection process included a review of portions of an issuer audit completed by the Firm. This review was intended to identify whether deficiencies existed in those portions of the inspected audit, and whether such deficiencies indicated defects or potential defects in the Firm's system of quality control over audits. In addition, the inspection included reviews 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.

PROFILE OF THE FIRM¹

Number of offices	1 (Mesa, Arizona)
Ownership structure	Sole proprietorship
Number of partners	1
Number of professional staff ²	1
Number of issuer audit clients	1
Other names used in audit reports	Shelley International CPA 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.

³ The Firm filed a special report on PCAOB Form 3 describing a change in its legal name from Shelley International CPA to Mark Shelley CPA, effective July 1, 2014.

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's inspection staff ("the inspection team") conducted primary procedures for the inspection from April 28, 2014 to May 2, 2014.⁴

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 standards that primarily relate to the deficiencies; they do not present a comprehensive list of every auditing standard that applies 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 the 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 of the 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 accordance with the applicable

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.

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.

The fact that one or more deficiencies in an audit reach this level of significance does not necessarily indicate that the financial statements are 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 –

Issuer A

- (1) the failure to perform sufficient procedures to test revenue, including the failure to identify certain risks of material misstatement at the assertion level (AS No. 12, paragraphs 59 and 68; AS No. 13, paragraphs 8, 13, and 36; AS No. 14, paragraphs 30 and 31; and AU 342, paragraphs .04 and .07);
- (2) the failure to perform sufficient procedures to test the existence and valuation of accounts receivable (AU 330, paragraph .31; AU 342, paragraph .10);

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 the inspections staff may include in its procedures monitoring or assessing a firm's compliance.

(3) the failure to perform sufficient procedures to evaluate whether goodwill was impaired (AS No. 13, paragraphs 8 and 36; AS No. 14, paragraph 3; AU 342, paragraphs .04 and .07);

(4) the failure to perform sufficient procedures to test the valuation of, and rights related to, long-lived assets (AS No. 13, paragraphs 8 and 36; AS No. 14, paragraph 30; AS No. 15 paragraph 10; and AU 334, paragraph .11); and

(5) the failure to perform sufficient procedures to identify related parties and related party transactions beyond those disclosed in the audited financial statements or to test the presentation and disclosure of related party transactions (AU 334, paragraphs .07 and .11).

B. Auditing Standards

Each deficiency discussed above could relate to several applicable provisions of the standards that govern the conduct of audits, including both the paragraphs of the standards that are cited at the end of each description of the deficiency included in Part I.A of this report and one or more of the specific paragraphs discussed below.

Many audit deficiencies involve a lack of due professional care. AU 230, *Due Professional Care in the Performance of Work* ("AU 230"), paragraphs .02, .05, and .06, requires the independent auditor to plan and perform his or her work with due professional care and sets forth aspects of that requirement. AU 230, paragraphs .07 through .09, and Auditing Standard ("AS") No. 13, *The Auditor's Responses to the Risks of Material Misstatement* ("AS No. 13"), paragraph 7, 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 No. 13, paragraphs 3, 5, and 8, requires the auditor to design and implement audit responses that address the risks of material misstatement, and AS No. 15, *Audit Evidence* ("AS No. 15"), paragraph 4, 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 support of the related conclusions.

The table below lists the specific auditing standards that are referenced for each deficiency included in Part I.A of this report. See the descriptions of the deficiencies in Part I.A for identification of the specific paragraphs, in addition to those noted above, that relate to the individual deficiencies. Standards discussed above are cited again in the table only if the particular deficiency relates to aspects of the standard that are not discussed above.

PCAOB Auditing Standards	Issuer
AS No. 12, <i>Identifying and Assessing Risks of Material Misstatement</i>	A
AS No. 13, <i>The Auditor's Responses to the Risks of Material Misstatement</i>	A
AS No. 14, <i>Evaluating Audit Results</i>	A
AS No. 15, <i>Audit Evidence</i>	A
AU 330, <i>The Confirmation Process</i>	A
AU 334, <i>Related Parties</i>	A
AU 342, <i>Auditing Accounting Estimates</i>	A

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

Board inspections include reviews of certain portions of selected audit work performed by the inspected firm and reviews of certain aspects of the firm's quality control system. The inspections are designed to identify deficiencies in audits 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 failures to perform, or to perform sufficiently, certain necessary audit procedures. The inspection may not involve the review of all of a 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.

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 applicable accounting principles, 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.

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 No. 3, *Audit Documentation* ("AS No. 3"), 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, the inspection team considers whether audit documentation or any persuasive other evidence that a firm might provide to the inspection team supports a 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.

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.

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.

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

⁸ Not every audit deficiency suggests a defect or potential defect in a firm's quality control system.

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.

performance, training, compliance with independence standards, client acceptance and retention, and the establishment of policies and procedures.

END OF PART I

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. 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.

Mark Shelley CPA
1012 S. Stapley Dr. Suite 114
Mesa, AZ 85204
Phone: 480-461-8301
480-649-0622

January 12, 2015

Ms. Helen A. Munter
Director, Division of Registration and Inspections
1666 K. Street, N.W.
Washington, DC 20006
sent via fax: 202-862-8433

RE: Response to draft inspection report

Dear Ms. Munter:

We are pleased to respond to the Public Company Accounting Oversight Board's (PCAOB) 2015 draft report on the inspection of our firm, Mark Shelley CPA. We are committed to high audit quality and have designed our quality control systems to ensure and continually improve our audit methodology. We support the PCAOB's inspection process and believe that this process enhances our ability to evaluate and improve audit quality.

We acknowledge the professionalism of the PCAOB inspectors and appreciate their views regarding our audits. We recognize that inspection comments may reflect differences between professional judgments on accounting and auditing issues that were made during the course of our audits and those made by the PCAOB inspectors during the course of their inspections. Those differences may involve the nature and extent of audit documentation. Experienced, professionals can take differing approaches to achieve a high quality audit in accordance with professional standards.

After considering the inspection comments, we have begun to make adjustments to our audit procedures and documentations and will continue this improvement on a go-forward basis.

Sincerely,

A handwritten signature in black ink, consisting of a stylized 'M' and 'S' followed by a horizontal line.

Mark Shelley CPA

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>.

AS No. 12, Identifying and Assessing Risks of Material Misstatement		
Identifying and Assessing the Risks of Material Misstatement		
AS No. 12.59	The auditor should identify and assess the risks of material misstatement at the financial statement level and the assertion level. In identifying and assessing risks of material misstatement, the auditor should: a. Identify risks of misstatement using information obtained from performing risk assessment procedures (as discussed in paragraphs 4-58) and considering the characteristics of the accounts and disclosures in the financial statements. Note: Factors relevant to identifying fraud risks are discussed in paragraphs 65-69 of this standard. b. Evaluate whether the identified risks relate pervasively to the financial statements as a whole and potentially affect many assertions. c. Evaluate the types of potential misstatements that could result from the identified risks and the accounts, disclosures, and assertions that could be affected. Note: In identifying and assessing risks at the assertion level, the auditor should evaluate how risks at the financial statement level could affect risks of misstatement at the assertion level.	Issuer A

	d. Assess the likelihood of misstatement, including the possibility of multiple misstatements, and the magnitude of potential misstatement to assess the possibility that the risk could result in material misstatement of the financial statements. Note: In assessing the likelihood and magnitude of potential misstatement, the auditor may take into account the planned degree of reliance on controls selected to test.³² e. Identify significant accounts and disclosures³³ and their relevant assertions³⁴ (paragraphs 60-64 of this standard). Note: The determination of whether an account or disclosure is significant or whether an assertion is a relevant assertion is based on inherent risk, without regard to the effect of controls. f. Determine whether any of the identified and assessed risks of material misstatement are significant risks (paragraphs 70-71 of this standard).	
<u>Footnotes to AS No. 12.59</u> ³² Paragraphs 16-35 of Auditing Standard No. 13. ³³ Paragraph A10 of Auditing Standard No. 5 states: An account or disclosure is a significant account or disclosure if there is a reasonable possibility that the account or disclosure could contain a misstatement that, individually or when aggregated with others, has a material effect on the financial statements, considering the risks of both overstatement and understatement. The determination of whether an account or disclosure is significant is based on inherent risk, without regard		

to the effect of controls.		
³⁴ Paragraph A9 of Auditing Standard No. 5 states: A relevant assertion is a financial statement assertion that has a reasonable possibility of containing a misstatement or misstatements that would cause the financial statements to be materially misstated. The determination of whether an assertion is a relevant assertion is based on inherent risk, without regard to the effect of controls.		
Factors Relevant to Identifying Fraud Risks		
AS No. 12.68	<i>Presumption of Fraud Risk Involving Improper Revenue Recognition.</i> The auditor should presume that there is a fraud risk involving improper revenue recognition and evaluate which types of revenue, revenue transactions, or assertions may give rise to such risks.	Issuer A
AS No. 13, The Auditor's Responses to the Risks of Material Misstatement		
Responses Involving the Nature, Timing, and Extent of Audit Procedures		
AS No. 13.8	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.	Issuer A
Responses to Fraud Risks		
AS No. 13.13	<i>Addressing Fraud Risks in the Audit of Financial Statements.</i> 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	Issuer A

	standard, the auditor should perform tests of those controls.	
Substantive Procedures		
AS No. 13.36	The auditor should perform substantive procedures for each relevant assertion of each significant account and disclosure, regardless of the assessed level of control risk.	Issuer A
AS No. 14, <i>Evaluating Audit Results</i>		
Evaluating the Results of the Audit of Financial Statements		
AS No. 14.3	In forming an opinion on whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework, the auditor should take into account all relevant audit evidence, regardless of whether it appears to corroborate or to contradict the assertions in the financial statements.	Issuer A
Evaluating the Presentation of the Financial Statements, Including the Disclosures		
AS No. 14.30	The auditor must evaluate whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework. Note: AU sec. 411, <i>The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles</i>, establishes requirements for evaluating the presentation of the financial statements. Auditing Standard No. 6, <i>Evaluating Consistency of</i>	Issuer A

	<i>Financial Statements</i>, 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.	
AS No. 14.31	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 AU sec. 508, 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	Issuer A

	as appropriate by a specific auditing standard. ¹⁸	
<u>Footnote to AS No. 14.31</u>		
¹⁸ AU secs. 508.41-.44.		
AS No. 15, <i>Audit Evidence</i>		
Sufficient Appropriate Audit Evidence		
AS No. 15.10	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 No. 15.10</u>		
³ When using the work of a specialist engaged or employed by management, <u>see</u> AU sec. 336, <i>Using the Work of a Specialist</i> . When using information produced by a service organization or a service auditor's report as audit evidence, <u>see</u> AU sec. 324, <i>Service Organizations</i> , and for integrated audits, <u>see</u> Auditing Standard No. 5, <i>An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements</i> .		
AU 330, <i>The Confirmation Process</i>		
Alternative Procedures		
AU 330.31	When the auditor has not received replies to positive confirmation requests, he or she should apply alternative procedures to the nonresponses to obtain the evidence	Issuer A

	necessary to reduce audit risk to an acceptably low level. However, the omission of alternative procedures may be acceptable (a) when the auditor has not identified unusual qualitative factors or systematic characteristics related to the nonresponses, such as that all nonresponses pertain to year-end transactions, and (b) when testing for overstatement of amounts, the nonresponses in the aggregate, when projected as 100 percent misstatements to the population and added to the sum of all other unadjusted differences, would not affect the auditor's decision about whether the financial statements are materially misstated.	
AU 334, Related Parties		
Audit Procedures		
AU 334.07	The auditor should place emphasis on testing material transactions with parties he knows are related to the reporting entity. Certain relationships, such as parent-subsidary or investor-investee, may be clearly evident. Determining the existence of others requires the application of specific audit procedures, which may include the following: a. Evaluate the company's procedures for identifying and properly accounting for related party transactions. b. Request from appropriate management personnel the names of all related parties and inquire whether there were any transactions with these parties during the period.	Issuer A

	c. Review filings by the reporting entity with the Securities and Exchange Commission and other regulatory agencies for the names of related parties and for other businesses in which officers and directors occupy directorship or management positions. d. Determine the names of all pension and other trusts established for the benefit of employees and the names of their officers and trustees.⁴ e. Review stockholder listings of closely held companies to identify principal stockholders. f. Review prior years' working papers for the names of known related parties. g. Inquire of predecessor, principal, or other auditors of related entities concerning their knowledge of existing relationships and the extent of management involvement in material transactions. h. Review material investment transactions during the period under audit to determine whether the nature and extent of investments during the period create related parties.	
<u>Footnote 4 to AU 334.07</u> ⁴ According to FASB Statement No. 57, paragraph 24(f) [AC section R36.406] "trusts for the benefit of employees, such as pension and profit-sharing trusts that are managed by or under the trusteeship of management," are related parties.		
AU 334.11	For each material related party transaction (or aggregation of similar transactions) or common ownership or management control relationship for which	Issuer A

	FASB Statement No. 57 [AC section R36] requires disclosure, the auditor should consider whether he has obtained sufficient appropriate evidential matter to understand the relationship of the parties and, for related party transactions, the effects of the transaction on the financial statements. He should then evaluate all the information available to him concerning the related party transaction or control relationship and satisfy himself on the basis of his professional judgment that it is adequately disclosed in the financial statements. ⁸	
<u>Footnote 8 to AU 334.11</u> ⁸ The disclosure standards are contained in FASB Statement No. 57, paragraphs 2 through 4 [AC section R36.102-.104]. Also, see paragraph 31 of Auditing Standard No. 14, Evaluating Audit Results.		
AU 342, Auditing Accounting Estimates		
AU 342.04	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

Evaluating Accounting Estimates		
AU 342.07	The auditor's objective when evaluating accounting estimates is to obtain sufficient appropriate evidential matter to provide reasonable assurance that— a. All accounting estimates that could be material to the financial statements have been developed. b. Those accounting estimates are reasonable in the circumstances. c. The accounting estimates are presented in conformity with applicable accounting principles² and are properly disclosed.³	Issuer A
<u>Footnotes to AU 342.07</u> ² Section 411, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles, discusses the auditor's responsibility for evaluating conformity with generally accepted accounting principles. [Title of section 411 amended, effective for reports issued or reissued on or after June 30, 2001, by Statement on Auditing Standards No. 93.] ³ See paragraph 31 of Auditing Standard No. 14, <i>Evaluating Audit Results</i>.		
AU 342.10	In evaluating reasonableness, the auditor should obtain an understanding of how management developed the estimate. Based on that understanding, the auditor should use one or a combination of the following approaches: a. Review and test the process used by management to develop the estimate. b. Develop an independent expectation of the estimate to corroborate the reasonableness of management's estimate. c. Review subsequent events or	Issuer A

	transactions occurring prior to the date of the auditor's report. Note: When performing an integrated audit of financial statements and internal control over financial reporting, the auditor may use any of the three approaches. However, the work that the auditor performs as part of the audit of internal control over financial reporting should necessarily inform the auditor's decisions about the approach he or she takes to auditing an estimate because, as part of the audit of internal control over financial reporting, the auditor would be required to obtain an understanding of the process management used to develop the estimate and to test controls over all relevant assertions related to the estimate.	
--	---	--