

# Gators electronic essay sample

[Finance](#)



Succint:

Gator Electronics Inc. ("Gator") is an electronics manufacturer that sells electronic products to third-party retail centers in approximately 100 countries. Gator is an SEC registrant. You are planning to audit the current-year goodwill impairment analysis of Gator. Gator has performed its annual goodwill impairment analysis as of December 31, 20X3, with the assistance of an external valuation specialist, Management's Expert. Gator elected not to perform the qualitative assessment for determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount and proceeded with Step 1 of the quantitative two-step goodwill impairment test for all reporting units. On the basis of the valuation prepared by Management's Expert, Gator estimated that the fair value of all of the reporting units exceeded their respective carrying values and no Step 2 analysis was required or prepared. The focus of this case study will be on the U. S. reporting unit. The engagement partner has asked you to review Gator's discounted cash flow analysis (part of Step 1 test in determining fair value of the reporting unit) to determine what audit procedures should be performed.

Auditing and reporting issues:

Due to the complexity of performing the annual goodwill impairment testing, most companies engage valuation specialists to conduct the analysis. The auditors also rely on the help of the valuation specialist to evaluate the underlying data and assumptions. In this cases a misstatement arising primarily from recent market declines, the engagement partner has

determined that goodwill for the US reporting unit is a material account balance as of December 31, 20X3 because it is quantitatively significant (\$280 million) and qualitatively significant. The engagement partner has asked you to review Gator's discounted cash flow analysis to determine what audit procedure should be performed. Reporting issues:

- The qualitative assessment and evaluation process aims to reduce both the cost and complexity of goodwill impairment testing. However, such and assessment can be complicated, particularly when it is conducted amid continued global economic uncertainty and a volatile stock market that might not necessarily reflect the actual value of the company.
- The Discounted Cash Flow method is based upon forward-looking data and therefore requires a relatively large amount of predictions for the future business situation of the company and the economy in general. Minor changes in the underlying assumptions will result in large differences in the company's value. It is therefore very important to know which assumptions are used and how they influence the outcome of the analysis.
- The use of a pro-forma financial statement: Pro-forma balance sheets are created by forecasting the company account balances at a future date and then aggregating them into a financial statement format. Account balances are forecasted by identifying the forces that influence them and projecting how the accounts will be influenced in the future by such forces. Pro forma statements are mostly based on assumed numbers. Because these are assumptions, full reliance on pro forma statements is not recommended.

Authoritative basis:

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-To mitigate the issue about the valuation we can start making referente to AU sec 328: 03. 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) Accounting Standards Codification (ASC) glossary term fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. 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.

06. Assumptions used in fair value measurements are similar in nature to those required when developing other accounting estimates. However, if observable market prices are not available, GAAP requires that valuation methods incorporate assumptions that marketplace participants would use in their estimates of fair value whenever that information is available without undue cost and effort. If information about market assumptions is not available, an entity may use its own assumptions as long as there are no contrary data indicating that marketplace participants would use different assumptions. These concepts generally are not relevant for accounting estimates made under measurement bases other than fair value. Section 342, Auditing Accounting Estimates, provides guidance on auditing accounting estimates in general. This section addresses considerations

similar to those in section 342 as well as others in the specific context of fair value measurements and disclosures in accordance with GAAP.

-To mitigate the risk about the valuation made by a valuation specialist AICPA disclosed in AU sec 328: Engaging a Specialist 21. When planning to use the work of a specialist in auditing fair value measurements, the auditor considers whether the specialist's understanding of the definition of fair value and the method that the specialist will use to determine fair value are consistent with those of management and with GAAP.

22. Section 336 provides that, while the reasonableness of assumptions and the appropriateness of the methods used and their application are the responsibility of the specialist, the auditor obtains an understanding of the assumptions and methods used. However, if the auditor believes the findings are unreasonable, he or she applies additional procedures as required in section 336.

Reporting on Pro Forma Financial Information: AT Section 401 04. The objective of pro forma financial information is to show what the significant effects on historical financial information might have been had a consummated or proposed transaction (or event) occurred at an earlier date. Pro forma financial information is commonly used to show the effects of transactions.

06. Pro forma financial information should be labeled as such to distinguish it from historical financial information. This presentation should describe the transaction (or event) that is reflected in the pro forma financial information, the source of the historical financial information on which it is based, the

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significant assumptions used in developing the pro forma adjustments, and any significant uncertainties about those assumptions. The presentation also should indicate that the pro forma financial information should be read in conjunction with related historical financial information and that the pro forma financial information is not necessarily indicative of the results (such as financial position and results of operations, as applicable) that would have been attained had the transaction (or event) actually taken place earlier.

The practitioner's report on pro forma financial information should be dated as of the completion of the appropriate procedures. The practitioner's report on pro forma financial information may be added to the practitioner's report on historical financial information, or it may appear separately. If the reports are combined and the date of completion of the procedures for the examination or review of the pro forma financial information is after the date of completion of the fieldwork for the audit or review of the historical financial information, the combined report should be dual-dated. (For example, " February 15, 20X2, except for the paragraphs regarding pro forma financial information as to which the date is March 20, 20X2.")

Recommendation:

Improve risk assessment procedure to identified fraud or misstatement in the financial information. AU-C Sec 315:

Perform risk assessment procedures to provide a basis for the identification and assessment of risks of material misstatement at the financial statement and relevant assertion levels. Risk assessment procedures by themselves, however, do not provide sufficient appropriate audit evidence on which to base the audit opinion. The risk assessment procedures should include the <https://assignbuster.com/gators-electronic-essay-sample/>

following: a. Inquiries of management and others within the entity who, in the auditor's professional judgment, may have information that is likely to assist in identifying risks of material misstatement due to fraud or error. b. Analytical procedures.

c. Observation and inspection.

Improve the understanding of the pro-forma statement to identified errors in the valuation. AU-C Sec 540:

The auditor should obtain sufficient appropriate audit evidence about whether the disclosures in the financial statements related to accounting estimates are in accordance with the requirements of the applicable financial reporting framework. For accounting estimates that give rise to significant risks, the auditor also should evaluate the adequacy of the disclosure of estimation uncertainty in the financial statements in the context of the applicable financial reporting framework.