Green: financial statements and subsequent events essay

Green, CPA, is auditing the financial statements of Taylor Corporation for the year ended December 31, 20X1.

Green plans to complete the fieldwork and sign the auditor's report about May 10, 20X2. Green is concerned about events and transactions occurring after December 31, 20X1, that may affect the 20X1 financial statements. a. What are the general types of subsequent events that require Green's consideration and evaluation? According to the American Institute of Certified Public Accountants, " an independent auditor's report ordinarily is issued in connection with historical financial statements that purport to present financial position at a stated date and results of operations and cash flows for a period ended on that date" (AICPA, 2006). However, according to past experience, there have proven to be many events or transactions that sometimes occur after the balance-sheet date, but prior to the issuance of the financial statements that can have a material effect on the financial statements themselves, subsequently requiring an adjustment or disclosure in the statements. These occurrences, according to the AICPA are referred to as " subsequent events," may require dollar adjustments to the financial statements and/or disclosure" (AICPA, 2006). AICPA literature identifies " two types of subsequent events – Type I and Type II" (AICPA, 2006).

Type I subsequent events provide evidence about conditions that existed at the balance sheet date. Examples of a Type I subsequent event can take the form of a lawsuit being settled for a different amount than was accrued, or the client issuing a stock dividend or declaring a stock split during the subsequent period. In both cases, the auditor is required to adjust the financial statement figures to reflect the impact of these events. Footnote disclosure might also be required in many cases to provide additional information to interested parties. Type II subsequent events indicate conditions that did not exist at the alance sheet date but may require disclosure. According to current AICPA regulations, “ the financial statement account balances should not be adjusted for these events, but they should be considered for disclosure’ (AICPA, 2006). The following are examples of Type II subsequent events: an uninsured casualty loss that occurred after the balance sheet date that causes a customer’s bankruptcy resulting in a high probability that repayment of a debt may not occur, or a significant lawsuit is initiated against the client relating to an incident that occurred after the balance sheet date.

What are the auditing procedures Green should consider performing to gather evidence concerning subsequent events? When there has been an occurrence of a subsequent event, and the appropriate financial statement has been modified to reflect the change (along with all necessary notes and/or disclosures), the auditor has two options for dating the report (Rittenberg and Schwieger, 2005): 1. Use the date of the event as the date of the audit report. 2. Dual date” the report, using the dates of the end of the fieldwork and the date of the event, to disclose the work done only on that event after the completion of fieldwork. To an auditor the use of the proper option for dating his or her report is extremely important in determining liability in the event that an additional subsequent event occurs after the audit report has been issued. For example, consider a situation where the auditor completed the audit on February 12, 2007. A fire then destroys the client’s main factory on February 24, 2007. The unfortunate event is disclosed by the auditor in Note 12 to the company's financial statements, with the report being issued to the client on March 5.

The auditor in such a case can date the report March 2, 2007 or dual-date it as February 12, 2007 (the date when the original audit was completed), except for Note 14, which is dated February 24, 2007 (the date of the subsequent event). By dual-dating the report, the auditor is assuming less responsibility, as the only event that occurred after the end of the original fieldwork was the subsequent event is property disclosed in Note 14. If on the other hand, the auditor dated his or her report February 24, 2007, the auditor would be taking full responsibility for all events (discovered and undiscovered) that might have occurred from February 12 to March 5, 2007. Needless to say, it behooves an auditor to properly date his or her report. References: AICPA, (2006).

AU section 560 – subsequent events. Retrieved November 7, 2007, from AICPA Web site: http://www. aicpa.

org/download/members/div/auditstd/AU-00560. PDF Rittenberg, L, ; Schwieger, B (2005). Auditing concepts for a changing environment. Mason, OH: Thomson South-Western