

Using Role Play as an Experiential Learning Tool to Introduce Students to Auditing

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Abstract

This paper examines the impact of exposing students to the complex constructs of auditing by engaging them in a role-playing exercise on the first day of class. The exercise is designed to demonstrate the value-added nature of the audit process and the nature of evidence gathering. Controlled experiments at a large educational institution confirm the overall objective. In particular, the results indicated that after the role-play, students better understood the audit environment, including an understanding of the types of evidence that may be involved in an audit, the different sources of evidence, the different degrees of reliability of internal and external evidence and the importance of the critical evaluation of evidence. Students learned that an audit is necessary to ascertain that there are no material errors or irregularities in the financial statements and that an audit provides reasonable assurance as to the fairness of the financial statements.

Introduction

Students are often challenged in the early days of the first auditing course to identify the classic roles and responsibilities of all the participants in the audit process. Faculty, on the other hand, has the opportunity to help their students clarify these roles and responsibilities through various pedagogical approaches. The authors developed a short (40 to 65 minutes) experiential learning role play case to illustrate the audit process for their students. This role playing activity has been used to introduce students to auditing on the first day of class to both graduate and undergraduate students at three universities. It is a useful pedagogy to quickly clarify the purpose of an audit, the audit process, various types of evidence, and audit reporting. This role play case resulted in significant learning by students about the purpose of auditing, the audit process and the methods and types of audit evidence, all in the first hour of the first audit class.

Motivation for Study

The primary motivation for the development of this case was a frustration experienced by the faculty with the inability of a significant number of students to comprehend the general environment of auditing, the purpose of auditing and the roles of the participants in auditing until some weeks into the class. The faculty believed that if they could develop a role play in which all students participated in the general process of an audit on the first day of class, the students would have an anchor for accelerated learning and understanding of the various auditing concepts that would be introduced as the semester progressed.

Students are accustomed to problem-solving approaches that have discrete answers. The auditing course is inherently ambiguous to them. Pedagogically, the selection of a starting point for the introduction of auditing constructs varies. Auditing textbooks often begin with audit procedures first and then demonstrate how the results of each of these steps leads to the expression of an opinion. However, students are accustomed to problem-solving (one right answer) approaches in their past accounting courses. With auditing they are confronted with relatively ambiguous ranges of answers. Also, until students have developed some grasp of what the audit process involves, they appear to flounder in their ability to connect the concepts studied.

Accounting Profession Points the Way

The Accounting Education Change Commission's (AECC) Position Statement No. 1 states that:
Students must be active participants in the learning process, not passive recipients of information. They should identify and solve unstructured problems that require the use of multiple information sources. Learning by doing should be emphasized. [Sundem, 1999]

This challenge raises the necessity of accounting faculty to identify, experiment with and refine participatory approaches to auditing that challenge students' critical thinking skills to enhance the traditional lecture-based, problem-solving approaches frequently used in accounting education.

The Pathways Commission (2012, p119) also confirms the desirability of faculty who are involved in the development of teaching techniques and presentation and communication skills that involve the use of innovative teaching methods.

Learning Styles of Students

Prior research, such as Black (2010), states that today's college students are more collaborative in their learning styles and enjoy working on teams and in groups to solve a common problem. Due to their dependency on technology, and the speed with which they experience video games, they find traditional classroom lectures boring. These students are looking for interactive play that is enjoyable and they expect this in the college classroom. In addition, Munoz and Huser (2008), note that college students find one-way lectures, rote memorization and regurgitation of

isolated facts and terms to be tedious. This one-size-fits-all-classroom experience is no longer valuable to students and they are looking for an enhanced learning experience (Hawtrey, 2007). This is especially true in accounting education in which students need broad skill sets to succeed in the profession, and the lecture-based, problem oriented approach may no longer be adequate.

Experiential Learning as Pedagogy

Experiential learning is a pedagogy that is consistent with the Accounting Education Change Commission's suggestions and congruent with the learning styles of today's college students. Experiential learning is the incorporation of active, participative opportunities in a course and occurs when students are transformed from the role of passive listeners to that of active respondents (Hawtrey, 2007), thus taking a more active role in their education (Munoz and Huser 2008).

Prior studies assert that experiential learning can provide multiple benefits to students. Specht and Sandlin (1991) found that experiential learning resulted in longer retention of accounting constructs for students than retention by students exposed to traditional lecture/problem-solving methods. This was evidenced by comparing test scores. Other studies show that connections in the emotional and long-term career achievements of individuals are improved when experiential learning is used (Kolb, 1984). In a study by Lee and Moffeit, (1990), when students were provided a theoretical framework of internal auditing, enhanced educational effort of teaching was achieved.

Role Playing as a Form of Experiential Learning

Role-playing is one form of the many aspects of experiential learning. Role-play involves three steps: (1) preparation and instruction, (2) dramatic action and discussion, and (3) evaluation. Role-playing is usually an in-class exercise in which students assume different roles, where they can consider different alternatives and take action in an imaginary situation. The use of role-play as a pedagogy helps students develop communication skills, in addition to helping them consider actions and decisions on a personal level. Janvrin (2003) used role-play to examine internal controls and fraud detection concepts. Webb (2006) used open-ended scripts to replicate real world work and asked students to assume roles, working through the open-ended scripts. In this work, students were encouraged to be creative and original in playing out their roles.

The authors believed that role-playing could provide their students with a glimpse into the overall audit process. The role-play developed here provides students with a fun, yet insightful, introduction to the theoretical framework of auditing.

Objectives of the Role-Play

The goal and objectives of the role-play exercise on the first day of class stem from the frustrations the authors experienced attempting to introduce auditing in a lecture format. In general the goal was to provide a first hand experience with the various factors in a somewhat controlled environment. It is believed that this experience provides a frame of reference for the students throughout the course for exploring in depth, some of the topical areas of auditing.

Given the goal of providing a framework for building constructs, specific objectives were developed relating to the topical areas of auditing and experience the authors had with confusion with these topics in past audit classes.

The specific objectives of the role playing exercise include:

- Provide a realistic and robust illustration of the audit environment;
- Demonstrate the purpose of auditing;
- Provide a walk through experience of gathering and assessing audit evidence;
- Provide an experience of forming an opinion (comparing evidence against established criteria); and,
- Provide an experience using the opinion report.

These objectives form a base upon which to build the detailed course material for the rest of the term. This goal and these objectives formed the basis for the development of the case scenario which forms the structure of the role-play exercise.

The Role-Play Exercise

Background and Organization

The case consists of Beattyville Auto Parts Company ("Beattyville"), a three-year old business which anticipates needing an audit to secure a bank loan. A simplified set of financial statements (see Appendix #1) establishes the base from which to begin the role-play exercise and provides initial information the students can relate to from their experience in prior accounting courses. The roles established for the students include: the auditors; the corporate controller; the banker; the lawyer; and the county recorder. The faculty member guides the progress of the role-play exercise. Dividing the students into one of the specific roles provides each with a focus point for the role-play exercise. Students can either volunteer to play the various roles or be assigned to the roles by the instructor. The second approach is the more desired approach and the one used in the paper.

Preparation and Instruction

The Beattyville audit role-play is very simple and easy to use especially since it takes approximately 40-65 minutes. The ideal use is at the beginning of a semester especially at the first class meeting when the Auditing course is introduced to students. The role-play exercise requires approximately 15 minutes of instructor preparation time spent mainly reviewing notes and deciding how to assign roles to students. One advantage of the role-play is that students require zero minutes of preparation time to be able to effectively participate and benefit from the role-play.

Dramatic Action and Discussion

The instructor begins the role-play by asking the class for a definition of auditing and the steps that are involved in the audit process. The instructor then introduces the definition of auditing as follows:

Auditing is a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria and communicating the results to interested users (Louwers et al, 2013).

The instructor then identifies and discusses some of the key concepts such as “systematic process”, “objectively obtaining and evaluating evidence”, “assertions”, “established criteria”, “communicating the results”, and “interested users”, embedded in the definition.

The instructor moves the action along by asking the class about the process the auditor follows to find evidence and the different hierarchy of evidence (e.g., internal, external) available. The instructor directs discussion of the differences between internal and external evidence, including examples of each, and the types of evidence that tend to be more reliable. The instructor also reminds the class that the auditor has a responsibility to identify and detect errors and fraud in Beattyville's financial statements and cannot rely completely on management's assertions (internal evidence). Therefore, the auditor independently finds and evaluates such evidence to corroborate management's assertions. Beattyville's corporate controller (appointed by the instructor before class) provides the company's financial statements for the auditor as noted in Appendix #1. The instructor identifies and selects certain accounts (Cash, Building and Property, and Liabilities) to continue the role-play exercise.

The instructor directs the class to the first account on the statement of financial position, Cash. The auditor needs to determine if the balance is fairly stated so she contacts the banker to verify the amount. The banker produces a confirmation for the auditor verifying the outstanding cash balance at year end. The confirmation letter is provided in Appendix #2. The instructor informs students that confirmation letters are now obtained electronically from financial institutions. At this point, the students will notice a discrepancy between the cash balance per the client (Beattyville,) and the bank.

Students might note that it is possible that there were reconciling items such as deposits in transit on the bank reconciliation. However, the corporate controller assures the auditor that the bank reconciliation (not included in the role play), had no reconciling items. The instructor asks the students if the cash discrepancy is the result of an error or fraud in the accounting process and the action to be taken by the auditor. The assumption is that an error occurred which must be corrected to ensure the fairness of the financial statements, and so an adjusting journal entry needs to be proposed to correct the discrepancy. At this point the instructor should have a discussion with the class about Beattyville's responsibility for accepting and making all journal entry corrections. The proposed journal entry and the impact on Beattyville's financial statements are reflected in Appendix #3. The instructor can now ask students what impact that journal entry has had on Beattyville's financials.

The role-play action then moves to the Building and Property account. The auditors may have two concerns at this point – ownership/rights and valuation. To address the ownership concern, the auditor needs to verify that Beattyville owns the property and therefore finds it necessary to contact the county clerk to verify ownership. The county clerk provides a document showing that the building is actually owned by another party as shown in Appendix #4. The auditor contacts the owner and obtains a copy of a lease agreement with Beattyville as noted in Appendix #5. This raises another question for the instructor to ask the class. Since Beattyville does not own the building, should it be capitalized as shown on the balance sheet?

The students are then asked to evaluate the lease and determine if it should be treated as a capital or an operating lease. This requires the students to think back to the accounting for leases and the criteria used to determine the classification of a lease as provided in the accounting standards (FASB ASC 840-10-15). The lease criteria are reproduced for convenience in Appendix #6.

The students should realize that the lease is an operating lease since ASC 840-10-15 criteria were not met. This indicates that the lease was incorrectly classified by Beattyville. The students are then asked to propose the adjusting journal entry to be made by the auditor and determine its impact on the financial statements. The proposed adjusting journal entry and the revised financial statements are provided in Appendix #7. The valuation issues (i.e., depreciation) are excluded from the discussion for simplicity purposes. However, students are reminded that the capital asset would normally be depreciated therefore any previous depreciation charges would be reversed as part of any proposed solution.

Auditors are also concerned that the liabilities shown on the financial statement are complete since underreporting of liabilities will result in the overstatement of income. A particular area of concern is the identification of all contingencies. The instructor asks the students to recall the treatment of contingencies as provided in the accounting standards and to determine the rule for accruing versus disclosing a contingency. The Accounting for Contingencies is reproduced for convenience in Appendix #8. One source of contingencies is legal issues, so the auditor contacts the outside attorney to determine if there are any outstanding lawsuits or claims against the client. The attorney provides the auditor with a legal letter as reproduced in Appendix #9.

The students are asked to determine if an adjustment is necessary in light of the information provided by the attorney. They should realize that one is necessary since the two conditions for accruing a liability are met (i.e., probable and reasonably estimated), and an adjustment was not recorded by Beattyville. The required adjusting journal entry and the impact on Beattyville's financial statements are provided in Appendix #10.

Before the auditors can complete the audit and issue the report, they need to review the financial conditions and risk factors of the client, and evaluate whether it will be able to continue to operate in the future. This is the point in the role-play where the instructor introduces the 'going concern uncertainty' concept to the class. The students should be familiar with this concept from prior accounting classes (concept statements) and so this phase of the role-play should not be too challenging. The instructor could review the going concern criteria with the class if necessary, and these are available in Appendix #11. The instructor should also emphasize that the decision as to whether Beattyville is a going concern is not made by Beattyville, but by the auditors. The

going concern consideration is an auditing standard (SAS) followed by the auditors when conducting an audit. Here the instructor can also discuss the differences between the SASs (auditing standards) and the ASCs (accounting standards).

The students are then asked to review the revised Beattyville financial statements as noted in Appendix #10 and determine if the client can continue to operate as a going concern or if there is uncertainty about Beattyville's continued existence as a going concern. The students should recognize that conditions and events such as the negative equity, low asset values and high liability balances present a going concern uncertainty for Beattyville.

A natural next step after this discussion is the type of report that the auditor should issue on Beattyville. The instructor informs students of the different types of audit reports or opinions that the auditor could issue on a particular client. These audit opinions are reproduced in Appendix #12. After some discussion, the instructor points out that the unqualified ("clean") audit report will be issued for Beattyville with an additional paragraph added after the opinion paragraph to discuss the going concern uncertainty. The instructor explains the reason for issuing a clean audit report especially since errors were found in the financial statements and there is a going concern uncertainty at Beattyville. The errors were corrected, but Beattyville may not be able to pay its creditors.

The instructor concludes the dialogue by reminding students of the objectives of the role-play exercise. The objectives include demonstrating the purpose of auditing, providing a realistic illustration of the audit environment, and providing a walk through experience of gathering and assessing audit evidence.

Evaluation

The role-play exercise was assessed in an undergraduate auditing course at a regional state university during the fall 2009 semester. The students (n=34) agreed that the role-play exercise gave them a better understanding of the audit process. They felt that they had a better understanding of the level of evidence required in an audit as a result of the role-play. The students all agreed that an understanding of accounting concepts such as determining the appropriate adjusting journal entries was important in the audit process.

The effectiveness of the role-play exercise was further assessed in a graduate auditing course (n=76) at a private university in a large metropolitan area during the fall 2010. A pre- and post-test instrument was developed by the authors for this purpose. The instrument consisted of 14 questions (see Appendix #13) covering the key learning outcomes of the role-play exercise. A paired comparison on each question was used to study the learning effectiveness of the exercise at the 5% level. The study's results are provided in Table 1.

As noted from the results, questions 2 and 9 indicated that the students learned about the purpose of an audit as a result of the role play exercise. Also, questions 6, 8 and 13 indicated that the students learned about the process of an audit as a result of the role-play exercise. Finally, questions 4, 5 10 and 12 indicated that significant student learning took place about the various types of evidence an auditor might obtain to provide reasonable assurance as to the fairness of

the financial statements. These results support the anecdotal evidence obtained from using the role-play exercise at the undergraduate level.

The results noted in Table 1 have some limitations. For instance, the subjects were graduate students who attended a private university in a large metropolitan area. Also, more than 60% of those students were homogenous (Chinese nationals). As a result, the same learning might not take place in a different setting or with a different population.

Conclusion

The auditing course is quite divergent from other analytical accounting courses such as intermediate accounting and tax. The auditing course requires high level cognitive skills and judgments needed to make determinations about the sufficiency and appropriateness of evidence.

The role play exercise was developed to help students develop these skills. Evidence from the use of the role-play exercise suggests that participation provided students with an anchor for the audit process that minimizes the disorientation that is often encountered during the first few weeks of the audit course. Students had a better understanding of the audit environment, including an understanding of the types of evidence that may be involved in an audit, the different sources of evidence, the different degrees of reliability of internal and external evidence and the importance of the critical evaluation of evidence. Students learned that an independent audit is necessary to ascertain that there are no material errors or irregularities in the financial statements and that an audit provides reasonable assurance as to the fairness of the financial statements.

Role-playing is an effective pedagogical tool to help students acclimate to the types of situations they will face in auditing and the components of the overall audit process on the first day of class. This role-play can be referred to during the semester to anchor the students in the audit process.

Table 1 – Survey Results

Survey Questions	Df	Significance (2-tailed)
Q1: I think that the primary purpose of an external audit is to assure the accuracy of the numbers reported in the financial statements.	76	.116
Q2: I think that the primary purpose of an external audit is to determine if the financial statements follow accounting principles generally accepted in the United States for material amounts reported.	76	.029**
Q3: I think one of the responsibilities of the external auditor is to correct any misstatements discovered in the audit by recording the appropriate journal entry and adjusting the financial statements.	74	.241
Q4: Examples of evidence that can be useful to an auditor in an audit include: knowledge of ownership, such as a grant deed to a property, and contract agreements of leases.	75	.000**
Q5: An example of evidence that can be useful to an auditor in an audit includes: the calculations for warranty expense accruals prepared by management.	74	.030**
Q6: I think professional skepticism refers to the process of the external auditor performing economic analysis to determine if the financial performance of the company, based on the financial statements, is a good investment for the owners.	74	.030**
Q7: I think that if the correct debits and credits were applied to the financial statements AND if the financial statements are in balance, then external auditors generally trust that the financial statements are fairly presented.	76	.206
Q8: I think that the external auditor is responsible for settling any discrepancies, or misstatements, between the company's cash account balance and the company's bank statements.	76	.001**
Q9: I think one of the reasons a company seeks an external audit is to improve the credibility of the financial statements presented to potential creditors and investors in order to help them determine any strengths and/or weaknesses of the company's financial position.	76	.011**
Q10: An example of evidence that can be useful to an auditor in an audit includes: a lawyer's responses to inquiries made by the auditor about contingencies against the client.	76	.000**
Q11: I think that one of the responsibilities of the external auditor is to teach the management of the company and their internal accountants how to apply the accounting principles generally accepted in the United States to the books and records of the company.	76	.081
Q12: An example of evidence that can be useful to an auditor in an audit includes: external evidence such as cut-off bank statements and reconciliations.	76	.000**
Q13: I think that the external auditor goes directly to customers, suppliers, agents, legal counsel, and banks of the company to collect evidence ONLY if they receive approval from the company's management allowing them to do so.	75	.000**
Q14: When auditing financial statements, the external auditor assumes that the entity is a going concern.	76	.066

**These questions were significantly different at the 5% level, indicating significant learning on the part of students.

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Appendix #1

Beattyville Auto Parts Company
Statement of Financial Position (Pre Audit)
As of December 31, 20X1

Assets

Cash	\$ 20,000	
Accounts Receivable	60,000	
Inventory	40,000	
Building and Property	175,000	
Goodwill	15,000	
Total Assets		\$ <u>310,000</u>

Liabilities and Stockholders Equity

Accounts Payable	\$ 5,000	
Common Stock	50,000	
Retained Earnings	255,000	
Total Liabilities and Stockholders Equity		\$ <u>310,000</u>

Beattyville Auto Parts Company
Income Statement
For the 12 Months Ended As of December 31, 20X1

Sales	\$ 840,000	
Less Expenses	760,000	
Net Income		\$ <u>80,000</u>

Appendix #2

January 31, 20x2

GOFAR BANK

Home Town, USA

Per your request concerning the bank balance of our customer, BEATTYVILLE AUTO PARTS CO., its bank balance as of December 31, 20x1 was \$1,000.00.

Sincerely,

Bank President
Gofar Bank

Appendix # 3

Recommended Journal Entry:

(RE) Net Income	\$ 19,000	
Cash		\$19,000

Beattyville Auto Parts Company
Statement of Financial Position (Revised)
As of December 31, 20x1

Assets

Cash	\$ 1,000	
Accounts Receivable	60,000	
Inventory	40,000	
Building and Property	175,000	
Goodwill	15,000	
Total Assets		\$ <u>291,000</u>

Liabilities and Stockholders Equity

Accounts Payable	\$ 5,000	
Common Stock	50,000	
Retained Earnings	236,000	
Total Liabilities and Stockholders Equity		\$ <u>291,000</u>

Beattyville Auto Parts Company
Income Statement
For the 12 Months Ended December 31, 20x1

<u>Net Income</u>	\$ <u>61,000</u>
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Appendix #4

February 2, 20x2

**COUNTY CLERK'S OFFICE
REGISTRAR OF DEEDS
Home Town, USA**

Dear Auditors:

Per your request, the concerned property at 1200 Amboy Avenue in Home Town, USA is owned by Sophia Leasing, Inc.. Its **appraisal value is \$750,000**

Very truly yours,

COUNTY CLERK of
Home Town, USA

BEATTYVILLE AUTO PARTS COMPANY

Home Town, USA

RENT CONTRACT:

Beattyville Auto Parts Company and Sophia Leasing, Inc. do enter into this rent agreement, effective December 1, 20x8 to be paid on a monthly basis. This rent agreement can be terminated by Sophia Leasing at any time with 30 days notice. The amount of the rent shall be **\$7,000.00 per month.**

Jasper Jenkins,
President

Sophia Leasing, Inc.

Appendix #6

FASB ASC 840-10-15
“ACCOUNTING FOR LEASES”

FASB ASC 840-10-15 requires classifying leases as capital leases if the lease agreement meets at least one of the following criteria:

- A) Lease transfers ownership of property to Beattyville Auto Parts Company by the end of the lease term.
- B) Lease contains a bargain purchase option for Beattyville Auto Parts Company.
- C) The lease term is equal to 75% or more of the estimated economic life of the leased property.
- D) The present value of the minimum lease payments equals or exceeds 90% of the excess of the fair value of the leased property, using the lessee's incremental borrowing rate.

Appendix #7

Recommended Journal Entry:

Beginning RE (Error)	\$ 91,000	
Rent Expense (NI)	\$ 84,000 ¹	
Building & Property		\$175,000

Beattyville Auto Parts Company
Statement of Financial Position (Revised)
As of December 31, 20x1

Assets

Cash	\$ 1,000	
Accounts Receivable	60,000	
Inventory	40,000	
Building and Property	0	
Goodwill	15,000	
Total Assets		\$ <u>116,000</u>

Liabilities and Stockholders Equity

Accounts Payable	\$ 5,000	
Common Stock	50,000	
Retained Earnings	61,000	
Total Liabilities and Stockholders Equity		\$ <u>116,000</u>

Beattyville Auto Parts Company
Income Statement
For the 12 Months Ended December 31, 20x1

<u>Net Income</u>	\$ <u>(23,000)</u>
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¹ (\$7,000 per month multiply by 12 months)

Appendix #8

FASB ASC 450
“ACCOUNTING FOR CONTINGENCIES”

1. **Probable** – the future event is likely to occur
2. **Reasonably Possible** – the chance of the future event occurring is more than remote but less than likely
3. **Remote** – the chance of the future event occurring is slight

Note: If Probable, and the amount of loss can be reasonably estimated, it should be accrued. If a range is indicated, the lower end of the range is accrued, and the balance is disclosed. If Reasonably Possible, the amount should be disclosed only.

Appendix #9

February 6, 20x2

**LEGAL SERVICES OF
HOME TOWN, USA**

After careful consideration of your request for additional liability information on our client, BEATTYVILLE AUTO PARTS, CO., we estimate that due to its dispute with a former injured employee, BEATTYVILLE may be found liable for an additional \$110,000 (the actual medical costs) to \$2 million because of compensating damages for pain and suffering. The exact amount is not now determinable.

Sincerely,

M. Jones, Esquire

Legal Services of Home Town, USA

Appendix #10

Recommended Journal Entry:

(RE) Net Income	\$ 110,000	
Contingent Liability		\$110,000

Beattyville Auto Parts Company
Statement of Financial Position (Revised)
As of December 31, 20x1

Assets

Cash	\$ 1,000	
Accounts Receivable	60,000	
Inventory	40,000	
Building and Property	-0-	
Goodwill	15,000	
Total Assets		\$ <u>116,000</u>

Liabilities and Stockholders Equity

Accounts Payable	\$ 5,000	
Contingent Liability	110,000	
Common Stock	50,000	
Retained Earnings	(49,000)	
Total Liabilities and Stockholders Equity		\$ <u>116,000</u>

Beattyville Auto Parts Company
Income Statement
For the 12 Months Ended December 31, 20x1

<u>Net Income</u>	\$ <u>(133,000)</u>
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Appendix #11

SAS 126

**“THE AUDITOR’S CONSIDERATION OF AN ENTITY’S ABILITY TO CONTINUE AS
A GOING CONCERN”**

The auditor has a responsibility to evaluate whether there is substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time, not to exceed one year beyond the date of the financial statements being audited (or one year from the balance sheet date or longer if necessary).

If the entity is unable to continue to meet its obligations as they become due without a) substantial disposition of assets outside the ordinary course of business, b) or they are forced into significant restructuring of debt,

The auditor must use **JUDGMENT** in deciding whether to add a paragraph to the audit report that says “substantial doubt exists about the entity’s ability to continue as a going concern.”

Appendix #12

Unqualified Audit Report -- A "Clean Opinion" occurs when the auditor believes, after gathering enough evidence, that the financial statements of the client present fairly, in all material respects, the financial position as of the balance sheet date and the results of operations and cash flows, all presented in conformity with generally accepted accounting principles.

Qualified Audit Report -- A Qualified Opinion occurs when the auditor believes, after gathering enough evidence, that the financial statements of the client present fairly...**except for** the effects of the matter to which the qualification relates. This occurs when a) there is a departure from generally accepted accounting principles that is material or b) there is a lack of sufficient competent evidence or a restriction on the scope of the audit so that an unqualified opinion cannot be expressed.

Adverse Opinion -- An Adverse Opinion states that the financial statements **do not** present fairly the financial position or results of operations or cash flows in conformity with generally accepted accounting principles.

Disclaim Opinion -- A Disclaim Opinion states that the auditors **do not** express an opinion on the fairness of the entity's financial statements.

Appendix #13

Survey

Please answer the following questions by checking the appropriate box next to the question.

	Strongly Disagree	Disagree	Mildly Disagree	No Opinion	Mildly Agree	Agree	Strongly Agree
1- I think that the primary purpose of an external audit is to assure the accuracy of the numbers reported in the financial statements.							
2- I think that the primary purpose of an external audit is to determine if the financial statements follow accounting principles generally accepted in the United States for material amounts reported.							
3- I think one of the responsibilities of the external auditor is to correct any misstatements discovered in the audit by recording the appropriate journal entry and adjusting the financial statements.							
4- Examples of evidence that can be useful to an auditor in an audit include: knowledge of ownership, such as a grant deed to a property, and lease contract agreements.							
5- An example of evidence that can be useful to an auditor in an audit includes: the calculations for warranty expense accruals prepared by management.							
6- I think professional skepticism refers to the process of the external auditor performing economic analysis to determine if the financial performance of the company, based on the financial statements, is a good investment for the owners.							
7- I think that if the correct debits and credits were applied to the financial statements and if the financial statements are in balance, then external auditors generally trust that the financial statements are fairly presented.							
8- I think that the external auditor is responsible for settling any discrepancies, or misstatements, between the company's cash account balance and the company's bank statements.							
9- I think one of the reasons a company seeks an external audit is to improve the credibility of the financial statements presented to potential creditors and investors in order to help them determine any strengths and/or weaknesses of the company's financial position.							
10- An example of evidence that can be useful to an auditor in an audit includes: a lawyer's responses to inquiries made by the auditor about contingencies against the client.							
11- I think that one of the responsibilities of the external auditor is to teach the management of the company and their internal accountants how to apply the accounting principles generally accepted in the United States to the books and records of the company.							
12- An example of evidence that can be useful to an auditor in an audit includes: external evidence such as cut-off bank statements and reconciliations.							
13- I think that the external auditor goes directly to customers, suppliers, agents, legal counsel, and banks of the company to collect evidence only if they receive approval from the company's management allowing them to do so.							
14- When auditing financial statements, the external auditor assumes that the entity is a going concern.							

Name: _____

Biographies



Susanne O'Callaghan is a professor of accounting in the Lubin School of Business at Pace University in New York, NY. She earned her Ph.D. in Accounting at the University of Cincinnati. Susanne's major research interests are in auditing, financial reporting, artificial intelligence and government/nonprofit accounting, and pedagogy. Susanne has published in the *Journal of Accountancy*, *Management Accounting*, *Internal Auditor*, *The CPA Journal*, and other journals.



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