

<b>Fraud Risk Assessment</b>		
<b>Client:</b> <i>Keystone Computers &amp; Networks, Inc.</i>		<b>G-10 CA 8/14/X5</b>
<b>Financial Statement Date:</b> <i>12/31/X5</i>		
Procedure	Performed by	Comments
1. Consider the results of the discussion among engagement personnel about the risk of material misstatement due to fraud.	<u>CA</u>	<i>See G-21 for a description of the discussion.</i>
2. Consider results of inquiries of management about the risks of fraud and how they are addressed.	<u>CA</u>	
3. Consider the results of planning analytical procedures.	<u>CA</u>	
4. Consider the existence of fraud risk factors listed on G-30 through G-35.	<u>CA</u>	
5. Consider any other information that might be relevant to the risk of material misstatement due to fraud.	<u>CA</u>	
<b>Risks of Material Misstatement Due to Fraud</b>		
<i>Management may be motivated to misstate financial results due to impending sale of the company.</i>		
<b>Responses</b>		
<b>Overall Responses</b>		
<i>Risks were considered in staffing the engagement and determining the appropriate level of supervision.</i>		
<b>Alterations of the Nature, Timing and Extent of Procedures</b>		
<i>Risks were considered in designing audit procedures for sales and accounts receivable and inventories. (See R-6 and R-9.)</i>		
<i>Procedures were performed to address the risk of management override of internal controls. (See G-23–G-24.)</i>		

## Appendix 6C Problems

- 6C-1. The audit plan for the audit of Keystone Computers & Networks, Inc., appears on pages 223 through 225. Review each major section of the audit plan and briefly describe the purpose and content of the section. Organize your solution in the following manner:

Section	Purpose	Content
Objectives of the Engagement	To describe the services that are to be rendered to the client	The objectives are (1) audit of KCN's financial statements for the year ended 12/31/X5, and (2) issuance of a letter on compliance with covenants of the client's letter of credit agreement.

6C-2. In the audit plan for the audit of Keystone Computers & Networks, Inc., on page 224 there is a section on significant accounting and auditing matters. The first of the matters described in this section involves the appropriate accounting for the sale of extended warranty contracts. Research this accounting issue and write a brief memorandum for the working papers describing the issue and summarizing the appropriate method of accounting for the revenue received from these contracts.

6C-3. In the audit plan for the audit of Keystone Computers & Networks, Inc., on page 224 there is a section on significant accounting and auditing matters. The second matter described involves capitalizing the costs of developing a software program for sale.

*Required:*

- a. Research this issue and write a brief memorandum for the working papers describing the issue and summarizing the appropriate method of accounting for the development costs.
- b. Based on your research, describe the major audit issue that you believe will be involved in auditing the software development costs.

6C-4. A partially completed analytical ratios working paper for Keystone Computers & Networks, Inc., is presented on page 223.

*Required:*

- a. Complete the working paper by computing the financial ratios for 20X5.
- b. After completing part *a*, review the ratios and identify financial statement accounts that should be investigated because the related ratios are not comparable to prior-year ratios and industry averages.
- c. For each account identified in part *b*, list potential reasons for the unexpected account balances and related ratios.

