DEPARTMENT OF ACCOUNTING AND FINANCE
ACCG323 FINANCIAL ACCOUNTING THEORY AND PRACTICE
UNIT OUTLINE – SEMESTER 1, 2004

I. UNIT CONTENT

This unit is a combination of both financial accounting theory and practice at an advanced level. The objectives of the unit are for students to develop both their technical accounting skills through an understanding of selected accounting standards, and their ability to critically evaluate financial accounting information and standards through an understanding of the different theoretical and philosophical approaches to accounting. This unit also allows students to develop their generic skills, particularly their analytical, appreciative, routine and interpersonal skills. The unit requires students to read a series of papers/articles, prepare reports or critiques of those papers and present their ideas in both written and oral forms in class. This requirement provides students with the opportunity to develop their ability to analyse, reason logically, conceptualise and construct arguments (analytic skills), to think and act critically (appreciative skills), to write reports (routine skills) and to present, discuss and defend views (interpersonal skills). The reports/critiques are part of the formal progressive assessment of the unit, and assessment is based on both the technical content and generic skill demonstration.

The unit begins in week 1 with an introduction to the unit and a consideration of the nature of theory, i.e what is theory and why is theory useful? Approaches to theory construction will be outlined, and consideration will be given to the scientific method as a basis for obtaining a greater understanding of accounting practice, and its role in society. In week 2, we examine normative accounting theory. The essential elements of our conceptual framework are also considered, together with a number of examples that demonstrate how these elements can be used in practice. An historical overview of accounting theory is provided, with particular emphasis on the limitations of the existing historical cost system. We then evaluate normative accounting theory, and outlines of alternative accounting systems such as current purchasing power, current cost accounting and continuously contemporary accounting will be given.

In week 3 we examine positive accounting theory with the primary focus being on agency theory and the principal-agent relationship, and how accounting numbers affect both debt and equity contracts, as well as the politics of accounting standard setting. In week 4 we will explore the international harmonisation of accounting with particular reference to its benefits and the difficulties that are associated with implementing international accounting standards across countries and cultures characterised by differing levels of size and development.

In week 5, we will examine the ‘critical’ perspective in accounting by exploring accounting in a social, political and environmental context. Emphasis will be placed on social and environmental accounting and critical perspectives in the accounting literature such as a political economy of accounting. An overview will also be provided on gender based issues in the accounting profession.
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In week 6 we cover ethics in accounting, and examine current ethical frameworks for decision-making, and some of the different ways ethics in accounting can be compromised. Specific emphasis will be placed on recent corporate collapses that involved creative accounting techniques.

In week 7, students will learn how to account for employee benefits such as annual leave, sick leave, and long service leave, as well as disclosures associated with related parties. In week 8, we examine how to account for financial instruments such as convertible notes, futures contracts and interest rate swaps, and in particular the aspects of measurement used in the reporting of financial instruments.

In week 9 we examine the issue of the valuation of heritage assets, and biological assets such as agricultural products. This lecture also evaluates the technical requirements for expenditure carried forward with respect to exploration and development within the extractive industries, whilst in week 10 we examine accounting for both finance and operating leases. Week 11 is dedicated to the understanding of accounting for intangibles, with particular emphasis on research and development, goodwill and intellectual capital.

In week 12, we examine the technical requirements of accounting and reporting for general insurance activities, using values other than historic cost. The final lecture will involve a presentation by an external guest lecturer, and a brief revision and exam overview will be given.

II. UNIT STRUCTURE

The structure of the unit is a weekly two hour lecture and a weekly two hour small group tutorial. The unit relies heavily on assignment-based learning. In lectures, students are expected to grasp the main concepts and techniques that relate to the subject matter. In addition to the lecture materials it is expected that students will read specified references. Using the concepts and techniques presented in lectures or references, students are required to prepare solutions to weekly assignments.

Lecture material for each week will not be distributed in class but will be available online at the web addresses listed below or in ERIC, in the week before the lecture. It is the student's responsibility to obtain a copy of the lecture notes before class, in order to make the appropriate notes during lectures. The solutions to weekly assignment questions will be discussed in tutorials in the week following the designated lecture. It is expected that tutors will lead and manage the discussion of assignment questions and that students will actively participate in the tutorial setting. The tutorials should be viewed by students as an active forum for any problems or difficulties that they are experiencing with the subject matter. In addition to the lecture notes, at the end of each week of tutorials, copies of the solutions to practical accounting problems only from that tutorial will be placed:

(1) on the Online Teaching Facility ACCG323 webpage at http://online.mq.edu.au/public/ACCG323/ and
(2) on the Macquarie University Library ACCG323 reserve unit folder webpage at http://www.lib.mq.edu.au/resources/reserve/

For theory questions, students are expected to have obtained a good summary of the main issues from their own study and from the tutorial discussion. Please note: Hard copies of lecture notes and tutorial solutions will no longer be placed in ERIC.
Students who wish to complete additional exercises from the textbooks may attempt these questions and then visit lecturers and tutors during consultation hours to obtain access to (but not photocopy) the solutions.

An important objective of the unit is the development of the written and verbal communication skills of students, in line with the generic skills requirements set out by the university. For this purpose the unit contains an assessed multi-choice tests, (see III below), an assessed tutorial assignment, (see IV below) an assessed tutorial presentation (see V below) and an assessed ethics assignment (see VI below). Students who feel the need to improve their writing skills for assignment and examination purposes, are strongly encouraged to attend the Writing Skills Program run by the Centre for Open Education (9850-7470), as outlined on p.59 of the 2004 Undergraduate Handbook.

III. MULTI-CHOICE TEST'S

Each week there will be a short multi-choice test containing 10 questions that are to be completed at the end of each tutorial. The total assessment for the best 10 of the 12 tests will be 15% (1.5% each week) of the overall unit assessment. It is only possible to sit for these tests in your designated tutorial. If you do not attend, the test marks for that week are automatically forfeited. The test questions will be based on material learnt throughout the lecture and through the designated readings each week. The tests are to be undertaken closed book, with the exception of the Accounting Handbook, which you can use. Tutors will collect the tutorial tests at the end of the tutorial, and students will mark them at the beginning of the next tutorial and then receive them back.

IV. TUTORIAL ASSIGNMENTS

During the semester tutors will collect your written assignments each week for the purpose of assessing whether or not you are making sufficient effort on the weekly assignments. This part of the assessment is worth 10%. Given that there are 12 tutorials, your best 10 will constitute the assessment. You will be graded either an “S” (satisfactory) which constitutes 1 mark or “U” (unsatisfactory) which constitutes 0 marks.

Once again it is only possible to submit your assignments in your designated tutorial. If you do not attend, the assignment marks for that week are automatically forfeited. No extensions will be granted by tutors for submitting the assignment late. Students absent from tutorials for medical reasons will be noted, and taken into account when determining your tutorial mark when appropriate medical evidence is produced.

Assignments may be checked for “copying” (within tutorials and across tutorials) and guilty parties (being the person/s who copied and the person/s who allowed the copying) will be subject to a detailed investigation by the Division. A reminder regarding plagiarism is attached as Appendix I.
V. TUTORIAL PRESENTATION

The unit also contains an assessed tutorial presentation worth 5% of the overall assessment (presentation to be marked out of 10). Each student is required to prepare a 5 minute (absolute maximum) presentation on an article or publication of interest to financial accountants, and the week of your presentation are to be organised by your tutor. Once again it is only possible to present your tutorial presentation in your designated tutorial. If you do not attend, the tutorial presentation mark for your designated week is automatically forfeited. The following list is provided as a guide on what to present:

- An article that has appeared in the journals of the Australian professional accounting bodies during the past 12 months, i.e., Charter or Australian CPA (available from the Library);
- An article that has appeared in an academic Australian accounting journal during the past 12 months, i.e., Australian Accounting Review, Accounting and Finance, Abacus, Accounting Forum or Accounting Research Journal (only the first three journals are available from the Library);
- An accounting based newspaper article located within either The Australian Financial Review or The Australian (the leading financial press) over the last 12 months.

Your audience may not be very familiar with the article or publication you have read. You are asked to take a “big picture” approach and present a simple overview of the main issues canvassed by the article. Do not simply read your written answer. Try to make it reasonably simple and interesting for your audience. It is expected that there will be 2 or 3 presentations in each tutorial with discretion left to tutors regarding the order of presentations. Notes or cards may be used during the presentation and the use of overheads is encouraged. Students are reminded that simply reading from pages of writing will result in nil marks.

According to Malouf (1990) there are ten major mistakes that speakers make when delivering. When delivering your presentation try not to fall into any of these mistakes:

- Failing to speak to time
- The material is not suited to the audience
- Information overload
- The material is too technical
- Poor preparation
- Failure to practice speech
- Distracting visuals/verbals/vocals
- Inappropriate pace
- Lack of eye contact
- Lack of enthusiasm

At the conclusion of all presentations students will receive an evaluation form from their tutors of their presentation providing feedback across a range of criteria and a mark out of 10. A copy of the presentation feedback form is attached at Appendix 2.

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VI. ETHICS CASE STUDY ASSIGNMENT

The unit contains an ethics case study assignment worth 15% of the overall assessment. The ethical case study will be distributed in the lecture prior to the mid-term break.

The assignment must not exceed 2,000 words in length. The assignment must be word-processed, double spaced, on one side only of A4 paper, and properly referenced including a bibliography. It is expected that assignments will be completed over the vacation period 12th April to 25th April. In the lecture week prior to the mid-term break, students will be provided with a framework for evaluating ethics. The ethical case study assignment is due for submission without exception on or before 6pm Tuesday 27th April (Monday 26th April is a Public Holiday for ‘Anzac Day’) and should be placed in a marked box inside ERIC. You must attach a cover sheet with your assignment, which is located at Appendix 3. A deduction of 25% on the total assignment mark will be imposed each day for late submission. Assignments will be marked out of 15, and guidance to the answer will be provided at the time of feedback.

It is expected that students will be aware of the appropriate standard for assignment writing at university (including how to reference the work of other authors). Without exception any evidence of plagiarism discovered in submitted assignments will result in a detailed investigation by the Division. A reminder regarding plagiarism is attached as Appendix 1 to this handout.

VII. UNIT ASSESSMENT

The following weightings apply for unit assessment:

<table>
<thead>
<tr>
<th>Component</th>
<th>%</th>
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</thead>
<tbody>
<tr>
<td>Multi-Choice Tests</td>
<td>15</td>
</tr>
<tr>
<td>Tutorial Assignments</td>
<td>10</td>
</tr>
<tr>
<td>Tutorial Presentation</td>
<td>5</td>
</tr>
<tr>
<td>Ethics Assignment</td>
<td>15</td>
</tr>
<tr>
<td>Final Examination</td>
<td>55</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
</tr>
</tbody>
</table>

Irrespective of accumulated marks, students must pass the final examination to gain a passing grade in this unit. Furthermore, irrespective of the total exam score, students must achieve satisfactory marks for each of the theoretical and the practical components of the final exam to pass the unit. The best preparation for the final exam is completion of the weekly tutorial assignments and the discussion of assignment questions in the tutorials. In adhering to divisional policy, dictionaries will not be allowed into the final exam. Marks will be awarded according to the following grading system as set out in the Bachelor Degree Rules 10(2);

<table>
<thead>
<tr>
<th>Grade</th>
<th>High Distinction (HD)</th>
<th>Distinction (D)</th>
<th>Credit (Cr)</th>
<th>Pass (P)</th>
<th>Conceded Pass (PC)</th>
<th>Fail (F)</th>
</tr>
</thead>
<tbody>
<tr>
<td>%</td>
<td>85-100</td>
<td>75-84</td>
<td>65-74</td>
<td>50-64</td>
<td>45-49</td>
<td>0-44</td>
</tr>
</tbody>
</table>

High Distinction: denotes performance which meets all unit objectives in such an exceptional way and with such marked excellence that it deserves the highest level of recognition.

Distinction: denotes performance which clearly deserves a very high level of recognition as an excellent achievement in the unit.
Credit: denotes performance which is substantially better than would normally be expected of competent students in the unit.

Pass: denotes performance which satisfies unit objectives.

Conceded Pass: denotes performance which meets unit objectives only marginally.

Fail: denotes that a candidate has failed to complete a unit satisfactorily.

Raw internal assessment and exam scores are an interim stage in determining your final Standardised Numerical Grade or SNG awarded to you. SNGs are a ranking of students based on all components of the unit assessment. They indicate that the students within that band have satisfied the necessary criteria for that band and have accordingly been allocated a numeric grade based on their performance within that band. There is no simple arithmetical relationship between raw marks and scaled marks. The relationship will almost always differ between units and between different performance bands within the same unit.

VIII. REQUIRED READINGS

Students must have a copy of the following books (all available in the bookshop). Both Deegan texts, along with the MaxMark Online Study Guide to accompany Deegan (three items), can be purchased as a package.

- Macquarie University, Booklet of Readings in ACCG323, 2004.

In addition, students should regularly read the financial press, in particular The Australian Financial Review and The Business Review Weekly (BRW) magazine, as the subject matter of this unit often comes up in topical business settings. This will broaden your understanding of the unit topics.
IX. STAFF

The full-time staff teaching on the unit is as follows:

<table>
<thead>
<tr>
<th>Name</th>
<th>Location</th>
<th>Contact No.</th>
<th>Role</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dr Lorne Cummings</td>
<td>C5C 428</td>
<td>9850-8531</td>
<td>Lecturer-in-charge and Tutor</td>
</tr>
<tr>
<td>Dr Elaine Evans</td>
<td>C5C 403</td>
<td>9850-6477</td>
<td>Lecturer and Tutor</td>
</tr>
<tr>
<td>Mr Indra Abeysekera</td>
<td>C5C 416</td>
<td>9850-7848</td>
<td>Lecturer, Unit Administrator and Tutor</td>
</tr>
<tr>
<td>Mr Philip Sinnadurai</td>
<td>C5C 427</td>
<td>9850-7101</td>
<td>Tutor</td>
</tr>
</tbody>
</table>

Tutorial lists will be placed on the notice board outside ERIC and on the Macquarie University Library ACCG323 reserve unit folder webpage at http://www.lib.mq.edu.au/resources/reserve/ on Friday March 5th, with tutorials beginning in the second week. Students who need to change tutorials should in the first instance seek to change their tutorial online in the first week, or if tutorials are full, to contact Mr Indra Abeysekera on address (jabeysek@efs.mq.edu.au) explaining the reason(s) for requesting a change as soon as possible. No tutorial changes will be allowed after the end of the second week. Any student experiencing problems of one sort or another may discuss the matter with their tutor or with the lecturer-in-charge.

All full time staff teaching on the unit are available for individual consultation with students for a designated 2 hours per week. A timetable of when these staff are available will be posted on the notice boards outside staff offices and on the reserve unit folder webpage via the library.
### X. SUMMARY OF ACCG323 PROGRAM SEMESTER 1 - 2004

<table>
<thead>
<tr>
<th>WEEK</th>
<th>DATES</th>
<th>LECTURE TOPIC</th>
<th>LECTURER</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>1 March</td>
<td>Overview of Accounting Theory (<em>No tute week 1</em>)</td>
<td>L. Cummings</td>
</tr>
<tr>
<td>2</td>
<td>8 March</td>
<td>Normative Accounting Theory</td>
<td>E. Evans</td>
</tr>
<tr>
<td>3</td>
<td>15 March</td>
<td>Positive Accounting Theory</td>
<td>L. Cummings</td>
</tr>
<tr>
<td>4</td>
<td>22 March</td>
<td>International Harmonisation of Accounting</td>
<td>E. Evans</td>
</tr>
<tr>
<td>5</td>
<td>29 March</td>
<td>Critical Dimensions in Accounting</td>
<td>L. Cummings</td>
</tr>
<tr>
<td>6</td>
<td>5 April</td>
<td>Ethics in Accounting</td>
<td>L. Cummings</td>
</tr>
</tbody>
</table>

**12th April to 25th April MID-SEMESTER RECESS (2 Weeks)**

<table>
<thead>
<tr>
<th>WEEK</th>
<th>DATES</th>
<th>LECTURE TOPIC</th>
<th>LECTURER</th>
</tr>
</thead>
<tbody>
<tr>
<td>7</td>
<td>26 April</td>
<td>Accounting for Employee Benefits and Related Party Disclosures</td>
<td>L. Cummings</td>
</tr>
<tr>
<td>8</td>
<td>3 May</td>
<td>Accounting for Financial Instruments</td>
<td>L. Cummings</td>
</tr>
<tr>
<td>9</td>
<td>10 May</td>
<td>Accounting for Heritage Assets, SGARA's and the Extractive Industries</td>
<td>L. Cummings</td>
</tr>
<tr>
<td>10</td>
<td>17 May</td>
<td>Accounting for Leases</td>
<td>L. Cummings</td>
</tr>
<tr>
<td>11</td>
<td>24 May</td>
<td>Accounting for Intangible Assets</td>
<td>I. Abeysekera</td>
</tr>
<tr>
<td>12</td>
<td>31 May</td>
<td>Accounting and Reporting of Insurance Activities</td>
<td>I. Abeysekera</td>
</tr>
<tr>
<td>13</td>
<td>7 June</td>
<td>Guest Lecturer and Revision</td>
<td>L. Cummings</td>
</tr>
</tbody>
</table>
DUE WEEK 2
OVERVIEW OF ACCOUNTING THEORY

Readings


Assignment Questions Due for Submission

1. Deegan (Financial Accounting Theory) – Ch. 1 – Question 1.3 (p.24)
2. Deegan (Financial Accounting Theory) – Ch. 1 – Question 1.4 (p.24)
3. Deegan (Financial Accounting Theory) – Ch. 1 – Question 1.5 (p.24)
4. Deegan (Financial Accounting Theory) – Ch. 1 – Question 1.6 (p.25)
5. Deegan (Financial Accounting Theory) – Ch. 1 – Question 1.7 (p.25)
6. Deegan (Financial Accounting Theory) – Ch. 1 – Question 1.10 (p.25)
7. Deegan (Financial Accounting Theory) – Ch. 1 – Question 1.12 (p.26)
8. Deegan (Financial Accounting Theory) – Ch. 1 – Question 1.14 (p.26)
9. Deegan (Financial Accounting Theory) – Ch. 1 – Question 1.16 (p.26)
10. Do you expect that we will ever have a single universally accepted theory of accounting, and if not, why not?
DUE WEEK 3
NORMATIVE ACCOUNTING THEORY

Readings

a) CPA Australia and ICAA, “Conceptual Framework for Accounting, SACs 1 through to 4”, in
b) Deegan, C., “Normative Theories of Accounting – the case of accounting for changing prices”,
c) Deegan, C., “Normative Theories of Accounting – the case of conceptual framework projects”,
d) Deegan, C., “An Overview of the Australian External Reporting Environment”, Chapter 1 in
f) Hampton, G. and Bishop, T., [1998], "Measurement and the Australian conceptual framework",
Australian Accounting Review, May, pp. 42-53.*

* - denotes article located in booklet of readings

Assignment Questions Due for Submission

1. Deegan – Financial Accounting Theory - Ch. 4 – Questions 4.3; 4.15; 4.16 (pp.125-127)
2. Deegan – Financial Accounting Theory - Ch. 5 – Questions 5.4; 5.5; 5.12 (pp.164-165)
3. Deegan – Australian Financial Accounting - Ch. 1 – Review Questions 8; 18; (p.51)
4. (refer to the Hampton & Bishop reading) In what ways are accounting numbers imprecise?
   What are the limitations of accounting numbers? How is the Australian conceptual framework
   related to measurement? What are the problems in relating measurement to the past and the
   future? For what purposes are the accounting numbers on a statement of financial position
   designed?
DUE WEEK 4
POSITIVE ACCOUNTING THEORY

Readings


Assignment Questions Due for Submission

1. Deegan (Financial Accounting Theory) – Ch. 7 – Question 7.1 (p.243)
2. Deegan (Financial Accounting Theory) – Ch. 7 – Question 7.2 (p.243)
3. Deegan (Financial Accounting Theory) – Ch. 7 – Question 7.3 (p.243)
4. Deegan (Financial Accounting Theory) – Ch. 7 – Question 7.6 (p.243)
5. Deegan (Financial Accounting Theory) – Ch. 7 – Question 7.9 (p.243)
6. Deegan (Australian Financial Accounting) – Ch. 2 – Review Question 9 (p.109)
7. Deegan (Australian Financial Accounting) – Ch. 2 – Review Question 17 (p.109)
8. Deegan (Australian Financial Accounting) – Ch. 2 – Review Question 23 (p.109)
9. Deegan (Australian Financial Accounting) – Ch. 2 – Review Question 28 (p.110)
10. Deegan (Australian Financial Accounting) – Ch. 2 – Challenging Question 31 (p.115)
DUE WEEK 5
INTERNATIONAL HARMONISATION OF ACCOUNTING

Readings


* - denotes article located in booklet of readings

Assignment Questions Due for Submission

1. Deegan – Financial Accounting Theory - Ch. 6 – Questions 6.4; 6.10; 6.13; 6.7 (pp.197-199)

2. Deegan – Australian Financial Accounting - Ch. 1 – Challenging Question 23 (p.58)

3. (refer to the AASB Policy Statement 4). Critically evaluate the benefits of convergence and harmonisation as outlined in para.7. Is it possible to demonstrate that these benefits will be achieved? What if they cannot be achieved?

4. (refer to the Ravlic & Hogan reading). Summarise the arguments for and against the decision to introduce international accounting standards in Australia by 2005. In your opinion, which person has the most persuasive argument, and why?

5. (refer to the Haswell & McKinnon article). The authors suggest that adoption of the IASB’s accounting standards will reduce the quality of financial reports in Australia. What evidence do they present to support this contention? Make an assessment of the validity of their claims in relation to politicisation of the process.

6. (refer to the Knapp article). Why did the ICAA come to the view that the AASB should be careful not to over-edit the text of the IASB standards? What role will there be for the AASB in the future?
DUE WEEK 6
CRITICAL DIMENSIONS IN ACCOUNTING

Readings


* - denotes article located in booklet of readings

Assignment Questions Due for Submission

1. Deegan – Ch. 9 – Question 9.1 (p.351)
2. Deegan – Ch. 9 – Question 9.7 (p.351)
3. Deegan – Ch. 9 – Question 9.13 (p.352)
4. Deegan – Ch. 9 – Question 9.18 (p.354)
5. Deegan – Ch. 12 – Question 12.2 (p.428)
6. Deegan – Ch. 12 – Question 12.6 (p.429)
7. Deegan – Ch. 12 – Question 12.10 (p.429)
8. (refer to the Baker and Bettner reading) According to the authors, why have interpretive and critical accounting articles not been published in leading academic accounting journals in the past? How has this restricted accounting, and what implications does a lack of academic focus
on critical accounting issues possibly have for the progress of accounting?

9. (refer to the Hines reading). From a socio-political context, what are 4 main problems that threaten the legitimacy of the accounting profession, and what role can the Conceptual Framework play in socialising/politicising the accounting profession?

10. (refer to the Lehman reading) Lehman states that from the perspective of accounting, feminism can be separated into three general classifications. Briefly describe these classifications, and outline how women have progressed in accounting through the different time frames of the 20th century (1900-1920, 1920-1940, 1940-1960, 1960-1980, the 1980's). In light of your own opinion, to what extent have women progressed in the last 10 years, and do the views of Lehman still have relevance today?

11. (refer to the Walters reading) To what degree do you think accounting firms should be restricted in the services that they provide to a particular client? Are the current problems in the accounting profession with respect to independence, a reflection of the failure of the accounting profession itself, or inherent in a system whereby audits are carried out by private organizations with a profit motive?
DUE WEEK 7
ETHICS IN ACCOUNTING

Readings


*  

c) Charles, E., [2002], “Bad Company”, Australian CPA, August, pp. 28-33. *

d) Cheney, G., [2002], “USA comes in from the cold”, Australian CPA, December, pp. 30-35. *


h) CPA Australia and ICAA, “Joint Code of Professional Conduct”, in Accounting and Auditing Handbook 2004 – Volume 2, Prentice-Hall. (Volume 2 is the Auditing Handbook for those students enrolled in ACCG340, or ACCG323 students can access the CPC online at the ACCG323 website).


* - denotes article located in booklet of readings

Assignment Questions Due for Submission

1. Why should members of the accounting profession act ethically?

2. “The fundamental duty of accountants is to clients or employees subject only to the public interest.’ Discuss the validity of this statement in relation to the Code of Professional Practice.

3. (refer to the Amat et al. reading).

   (a) Is creative accounting an illegal activity? What are the four methods of creative accounting according to Amat et al, and how can each be minimised?
(b) Why is creative accounting undertaken?

(c) What role does the market play in curbing creative accounting practices, and can the market always be relied upon to “sniff out” dubious accounting practices?

(d) Amat et al cites the work of Revsine who argues for a distinction between standard setting in the public and private sectors. Why is the distinction made, and how is the distinction linked to both the deontological and teleological viewpoints?

4. (refer to the “True and Fair is not hard and fast” reading) In the wake of some of the creative accounting incidences in the past, summarize the various proposals that the commentators advocate in the article.

5. (refer to the Charles reading) What was the central theme of the article with respect to the cause of many of the corporate collapses?

6. (refer to the Cheney reading) Cheney equates the corporate ethics crisis in the United States to that of a nuclear threat or environmental collapse. What does he mean by this?

7. (refer to the Dean reading) What is “low-balling”, and why is it undertaken? How can low-balling compromise the integrity of an audit?

8. (refer to the Fenwick Huss and Patterson reading) How can ethics be taught without imposing or indoctrinating value structures on students? Discuss this question in line with what you know about universalism and relativism. What role can ethics research play in the accounting education curriculum?

9. (refer to the Heathcote and James reading) Heathcote and James state that accounting practices are increasingly failing to reflect the “true and fair” value of businesses. Why is this so?

10. (refer to the Windsor reading) Windsor states of the ethics of selected auditors that “a small number are likely to act in their own self-interest and do the right thing only to avoid punishment”. Are there any limitations in applying the results of academic research to the actual behavior of the profession?

11. (Adapted from Henderson and Peirson, 2002, p.981) Michael Armstrong is an accountant with a small suburban practice. A significant proportion of his clients are medical practitioners, many of whom seem to be obsessed with avoiding taxes. One of his clients is Dr William Roberts, a very wealthy orthopaedic surgeon and the senior partner in a large practice, the partners of which are all clients of Armstrong. Dr Roberts approached Armstrong with a tax avoidance scheme which is ‘being widely used’ in the medical community. It involves selling accounts receivable at a discount to a financier. Roberts explains that the sale of assets at a loss does not incur tax, and as the revenue is never received from billings, there is no taxable income. When Armstrong expressed some doubts about the legality of the proposal, Roberts
argued that it was ‘perfectly legal’, was ‘widely used’ and if Armstrong was not prepared to implement it, Roberts and all his partners would ‘take their business elsewhere’.

**Required**

a) What risks would Armstrong run if he acceded to Roberts’ wishes?

b) What costs would Armstrong incur if he refused to accede to Roberts' wishes?

c) If Armstrong acceded to Roberts’ wishes, would there be a breach of the ASCPA Code of Professional Conduct, and under what sections?

d) What advice would you give to Armstrong?
DUE WEEK 8
ACCOUNTING FOR EMPLOYEE BENEFITS AND RELATED PARTY TRANSACTIONS

Readings

a) AASB 1017: Related Party Transactions
b) AASB 1028: Employee Benefits
e) Parker, D., [2001], “Fair Claim”, *Australian CPA*, December, p. 40. *
f) Wise, V., and Oliver, J., [2002], “Are employees entitled to more?”, *Australian CPA*, August, pp. 67-69. *

* - denotes article located in booklet of readings

Assignment Questions Due for Submission

1. Deegan – Ch. 12 – Review Question 2 (p.392)
2. Deegan – Ch. 12 – Review Question 10 (p.392)
3. Deegan – Ch. 12 – Review Question 13 (p.392)
4. Deegan – Ch. 24 – Review Question 5 (p.724)
5. Deegan – Ch. 24 – Review Question 10 (p.724)
6. Deegan – Ch. 24 – Review Question 11 (p.724)
7. Deegan – Ch. 12 – Review Question 15 (p.393). Assume however for this question that Jerry’s salary is $150,000 instead of $100,000, and that for part (b) Jerry takes three weeks annual leave instead of two, the tax increases to $3,000 instead of $1,200.
8. Deegan – Ch. 12 – Challenging Question 16 (p.393) Assume however that the weekly payroll is $380,000 instead of $300,000.
9. Deegan – Ch. 12 – Challenging Question 17 (p.393)
10. (refer to both the Parker and Wise & Oliver readings) Both readings comment on the ‘trust
funding model' (similar to that used to preserve superannuation entitlements) as a possible solution to employees missing out on their full employee entitlements when an employer organization becomes insolvent. Outline the advantages and disadvantages of such a trust funding model for companies that may be required to adopt such an approach.

11. In this problem, a reference to ownership relates to shareholdings. Aries Ltd owns 90% of Taurus Ltd, 60% of Gemini Ltd, 30% of Cancer Ltd and 21% of Leo Ltd. Assume that a shareholding of over 50% indicates control and a shareholding of over 20% indicates significant influence. (continued next page)

Directors of the companies are as follows:

<table>
<thead>
<tr>
<th>Company</th>
<th>Directors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aries Ltd:</td>
<td>Adam, Abraham and Anne</td>
</tr>
<tr>
<td>Taurus Ltd:</td>
<td>Tim and Tabatha (who are divorced)</td>
</tr>
<tr>
<td>Gemini Ltd:</td>
<td>George, Gillian and Graham</td>
</tr>
<tr>
<td>Cancer Ltd:</td>
<td>Charles and Caroline</td>
</tr>
<tr>
<td>Leo Ltd:</td>
<td>Liam and Lillian</td>
</tr>
</tbody>
</table>

Directors relatives include:

<table>
<thead>
<tr>
<th>Director</th>
<th>Relatives (relationship to Director)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tabatha</td>
<td>Robert (de facto)</td>
</tr>
<tr>
<td>Charles</td>
<td>Hannah (daughter)</td>
</tr>
<tr>
<td>Lillian</td>
<td>Stephen (husband)</td>
</tr>
<tr>
<td>Adam</td>
<td>Todd (nephew)</td>
</tr>
<tr>
<td>Abraham</td>
<td>William (brother)</td>
</tr>
<tr>
<td>George</td>
<td>Fleur (granddaughter)</td>
</tr>
<tr>
<td>Gillian</td>
<td>Esther (aunt)</td>
</tr>
</tbody>
</table>

Required

Identify the related parties of Taurus Ltd in accordance with AASB 1017, justifying your answer by reference to the relevant parts of the paragraph 9.1 related party definition.
12. Consider the following group structure in relation to X Pty Ltd and determine who are the identifiable related parties in accordance with AASB 1017;

```
W Plc
  /   \
/     \ 60%  25%
F Ltd  X Pty Ltd
  /     \\     \
 H Pty Ltd  Y Pty Ltd
           /  80%  25%
            \     \
             G Ltd I Pty Ltd
                  /  70%
                   Z Pty Ltd
```

*Additional Information:*
Each of the percentages shown above represent voting shares and each ownership interest is supported by proportional representation on the board of directors.

In addition to the interests shown above, X Pty Ltd is also the trustee of the X Pty Ltd Staff Superannuation Fund, which is an employer sponsored defined contribution fund (i.e. the earnings and capital growth from investments accumulate wholly to the members of the fund).

The directors of X Pty Ltd at 30 June 20X6 are Mike, Carol and Tiger. Mike and Carol have children from previous marriages, namely, Greg, Peter, Bobby, Marcia, Jan and Cindy. Alice and Sam are the original owners of X Pty Ltd business, and own the remaining 40% of the shares in X Pty Ltd. Kitty Carryall is a director of Z Pty Ltd.

Greg acts as X Pty Ltd’s solicitor, and the firm in which he is a senior partner provides legal services to X Pty Ltd on normal commercial terms. Tiger represents the company’s bankers, Parasite Ltd, on the board of directors. Parasite Ltd provides substantial funds to X Pty Ltd and its primary finance provider. Mike is known for his entrepreneurial flair and also acts as an independent director for Coles Myer Ltd and ICI Ltd.
DUE WEEK 9
ACCOUNTING FOR FINANCIAL INSTRUMENTS

Readings

a) AASB 1033: Accounting for Financial Instruments

* - denotes article located in booklet of readings

Assignment Questions Due for Submission

1. Deegan – Ch. 14 – Question 1 (p.439)
2. Deegan – Ch. 14 – Question 8 (p.439)
3. Deegan – Ch. 14 – Question 11 (p.440)
4. Deegan – Ch. 14 – Question 12 (p.440)
5. Deegan – Ch. 14 – Question 18 (p.440)
6. Deegan – Ch. 14 – Question 20 (p.441)
7. Deegan – Ch. 14 – Question 21 (p.441)
8. (refer to the Matolcsy and Petty reading) What were some of the concerns that the authors raised with respect to the corporate governance and disclosure issues related to the use of derivatives by Australian companies? For organisations that do engage in derivatives, what impact do these concerns have on the director’s ability to attest that financial statements are “true and fair”? 
9. An entity issued 2 000 000 convertible notes on 1 July 1996. The notes have a four year term, and were issued at $5 per note, giving total cash proceeds of $10 million. Interest is payable annually in arrears at a rate of 8% per annum. Each note is convertible into one ordinary share at or before maturity. When the notes were issued, the prevailing market interest rate for similar debt without conversion options attached was 9% per annum. 
(see next page).
Required:

a. Prepare the journal entries to record the issue of the convertible notes so as to enable the disclosures required under AASB 1033 ‘Presentation and Disclosure of Financial Instruments’.

b. Prepare the journal entries subsequent to issue, for the remaining 4 years, on the basis that conversion does not occur.

c. How does this treatment differ from the treatment suggested in SAC4 ‘Definition and Recognition of the Elements of Financial Statements’?
DUE WEEK 10
ACCOUNTING FOR HERITAGE ASSETS, SGARA’S AND THE EXTRACTIVE INDUSTRIES

Readings

a) AASB 1022: Accounting for the Extractive Industries

* - denotes article located in booklet of readings

**Assignment Questions Due for Submission**

1. Deegan – *Australian Financial Accounting* - Ch. 8 – Review Questions 3; 4; 8 (p.283).
2. Deegan – *Australian Financial Accounting* - Ch. 8 – Challenging Questions 14; 15 (p.284)
3. (refer to the Burritt and Cummings reading) Examine the valuations inherent in the “economic accounts” of Earth Sanctuaries Ltd prior to the adoption of AASB 1037 “Self-Generating and Re-Generating Assets” in 1999.
   a) What do the authors have to say with respect to the relevance and reliability of the asset figures contained in these “economic accounts”?
   b) Do you feel Earth Sanctuaries was justified in preparing these alternative “economic accounts” alongside conventional financial accounts? What was the company trying to achieve?
   c) Should endangered wildlife be allowed to be actively traded on an open market, and if so, would it protect endangered species and increase their numbers?
4. (refer to the Carnegie & Wolnizer reading). Evaluate C & W's argument that because public collections are valued for their cultural, heritage, scientific and educative qualities they cannot
be valued in monetary terms.

5. Deegan – Australian Financial Accounting - Ch. 19 – Review Questions 1; 2; 3; 7; 11; 15; 16 (pp. 605-608).
DUE WEEK 11
ACCOUNTING FOR LEASES

Readings

a) AASB 1008: Accounting for Leases

Assignment Questions Due for Submission

1. Deegan – Australian Financial Accounting - Ch. 10 – Review Questions 1; 2; 3; 7; 11; 13 (pp. 351-353).
DUE WEEK 12
ACCOUNTING FOR INTANGIBLE ASSETS

Readings

a) AASB 1011: Accounting for Research and Development Costs

* - denotes article located in booklet of readings

Assignment Questions Due for Submission

1. Deegan – Australian Financial Accounting - Ch. 7 – Review Questions 1; 4; 9; 13 (pp. 243-244).
2. (refer to the Powell reading)
   a) How does IAS 38 differentiate a cost as research or development for accounting purposes?
   b) How does IAS 38 approach recognizing internally developed intangible assets?
   c) How does IAS 38 approach recognizing goodwill?
   d) How does IAS 38 approach recognizing identifiable intangible assets?
3. (refer to the Abeysekera “All in the mind” reading)
   a) Which factors have brought intellectual capital to the forefront?
   b) What methods are available to quantify intellectual capital at the organizational level?, and why are they useful?
   c) (i) What methods are available to quantify intellectual capital within a firm?
      (ii) What are the two major problems of those methods quantifying intellectual capital within a firm?
   d) What are the four accounting elements of Intellectual Accounting Scorecard?, and how are they been defined?
4. (refer to the Abeysekera “Mind over matter” reading)
   a) Describe intellectual assets by internal, external, and human assets.
   b) Give examples of emotional assets.
   c) Why should firms pay attention to emotional assets?
   d) As an accountant how can you help firms to manage emotional assets to increase the market value of the firm?
DUE WEEK 13
ACCOUNTING AND REPORTING OF INSURANCE ACTIVITIES (FINAL TUTORIAL)

Readings

a) AASB 1023: Financial Reporting of General Insurance Activities
b) Carlin, T. M., [2002], Valuation Implications of Mark to Market Accounting in the General Insurance Industry, 9th World Congress of Accounting Historians Conference, Melbourne. *

* - denotes article located in booklet of readings

Assignment Questions Due for Submission

1. Deegan – Australian Financial Accounting - Ch. 20 – End-of-chapter exercise 1 (p.629).
3. (refer to the Carlin reading)
   a) What was the greatest emphasis of implementation of the provisions of the Insurance Act 1973?
   b) What were the two main objections raised by the audit/accounting profession to investment accounting provision of ED 43?
   c) What were the main conclusions of this study?
APPENDIX 1

THE DANGERS OF CHEATING AND PLAGIARISM AND HOW TO AVOID THEM

To cheat in the context of university assignments, tests and examinations is to attempt to gain an unfair advantage by violating the principles of intellectual and scholarly integrity. Cheating also encompasses plagiarism, which is the appropriation or imitation of another person’s ideas and manner of expressing them.

WHAT IS PLAGIARISM?

The Academic Senate in June 2001 approved policies and procedures to ensure that the University takes a consistent and equitable approach to plagiarism. The Senate adopted the following definition of plagiarism.

Definition: Plagiarism involves using the work of another person and presenting it as one's own. Any of the following acts constitutes plagiarism unless the source of each quotation or piece of borrowed material is clearly acknowledged.

a) copying out part(s) of any document or audio-visual material (including computer based material);

b) using or extracting another person's concepts, experimental results, or conclusions;

c) summarising another person's work;

d) in an assignment where there was collaborative preparatory work, submitting substantially the same final version of any material as another student.

Encouraging or assisting another person to commit plagiarism is a form of improper collusion and may attract the same penalties which apply to plagiarism.

Opportunities and temptations for plagiarism have increased with the spread of internet access. Plagiarism is a serious threat to the teaching and accreditation process, and seriously undermines the collegial and ethical principles which underpin the work of a University.

WHY IS IT WRONG?

If you take and use the work of another person without clearly stating or acknowledging your source, you are falsely claiming that material as your own work and committing an act of plagiarism. This is wrong because:

- it violates the principle of intellectual and scholarly integrity.
- it devalues the grades and qualifications gained legitimately by other students.
PREVENTING CHEATING

All students and staff have a responsibility to prevent, discourage and report cheating.

Typically students cheat because they are having difficulty with the unit content, the language of the unit, or both. Cheating and/or plagiarism can be a temptation when students are experiencing difficulty with a heavy workload in the unit and seek to save time by using others work.

To avoid having students resort to cheating, the University provides many services to help students with their course or to make thoughtful decisions about whether to continue. Within the Division of Economic and Financial Studies, students should first seek assistance from their tutor and/or lecturer. The University also offers help through the Dean of Students or the University Health and Counselling Services.

There is a difference between getting help and cheating. You are encouraged to get help if you need assistance to understand the material and any set work so that you are in a better position to create your own answers.

HOW TO PLAY IT SAFE

To maintain good academic practice, so that you may be given credit for your own efforts, and so that your own contribution can be properly appreciated and evaluated, you should acknowledge your sources and you should ALWAYS:

(i) State clearly in the appropriate form where you found the material on which you have based your work, using the system of reference specified by the Division in which your assignment was set;

(ii) Acknowledge the people whose concepts, experiments or results you have extracted, developed or summarised, even if you put these ideas into your own words;

(iii) Avoid excessive copying of passages by another author, even where the source is acknowledged. Find another form of words to show that you have thought about the material and understood it, but remember to state clearly where you found the ideas.

There is nothing wrong with working with other students in a group; indeed sometimes you will be encouraged to do so. But after a certain point, each student must work on their own to produce their own written answers. If no specific guidelines for group-work have been given, a reasonable interpretation is that it is acceptable for two or more students to discuss a problem among themselves or with a staff member. The group may then agree that the answer should include certain points. But then each member of the group must independently write their own answer to the problem.

PENALTIES

Offences of plagiarism will attract penalties which at a minimum, will result in the deduction of all marks for the test and/or assignment, to ultimately a failure in the unit and reference to the University Discipline Committee. The penalty will depend upon the extent of the plagiarism, whether it is a first or repeated offence, whether there is evidence of deliberate deceit and whether advantage has been taken of another student. In all cases however, a record of any offence and/or incident will be placed permanently on the students’ individual record file held at the university.
ACCG 340 - AUDITING AND ASSURANCE SERVICES

UNIT OUTLINE - SEMESTER 1, 2004
1. **UNIT DESCRIPTION**

This unit is primarily concerned with the external audit of corporate financial statements. The lectures presented are structured to correspond with audit methodology used in practice and integrate Australian and International Auditing Standards.

The majority of the lectures deal with the various activities undertaken by auditors. The main stages of the audit process are addressed including planning, gathering and evaluating audit evidence (including performance of tests of controls and substantive audit procedures) and the formation of the audit opinion. Topics such as analytical procedures and computer assisted audit techniques are not treated as separate topics, but are integrated throughout the unit. Other topics, including auditors' legal responsibilities, ethics and assurance services, are dealt with as special topics.

The lectures mainly deal with the concepts underlying the methodology, while the tutorial material is designed to demonstrate how the methodology is applied in practical situations.

2. **LECTURES**

Attendance at lectures is highly recommended. There will be practical explanations and examples given in lectures which supplement the text material and tutorial questions. If you choose not to attend lectures, it would be wise to be aware of any announcements made in lectures that could affect your study. Lecture notes will be available on the unit webpage and in ERIC a few days prior to the lecture. It is the students responsibility to download and print these notes.

3. **ASSESSMENT COMPONENTS**

<table>
<thead>
<tr>
<th>Component</th>
<th>Weight</th>
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</thead>
<tbody>
<tr>
<td>Mid-semester test (see note below)</td>
<td>35%</td>
</tr>
<tr>
<td>Final examination</td>
<td>65%</td>
</tr>
<tr>
<td></td>
<td>100%</td>
</tr>
</tbody>
</table>

To obtain a pass in the course, it is necessary to:
(a) attempt ALL assessment components, and
(b) obtain a pass in the final examination, and
(c) obtain an overall passing grade for the course.
6. **REFERENCE MATERIAL**

All students should purchase from the Co-op Bookshop the following:


The following texts are useful as additional references:


8. **UNIVERSITY STAFF**

James Hazelton (Lecturer in Charge)
Room: C5C 444
Phone: 9850 8486
Email: jhazelto@efs.mq.edu.au

Kym Boon (Unit Administrator)
Room: C5C 401
Phone: 9850 8451
Email: kboon@efs.mq.edu.au

Phil Ross
Room: C5C 412
Phone: 9850 8516
Email: phil.ross@efs.mq.edu.au

Chris Searchfield
Room: C5C 414
Phone: 9850 8462
Email: csearchf@efs.mq.edu.au

Please note that staff will only respond to emails that are sent by students from their Macquarie University email address.
iii) summarising another person's work;
iv) in an assignment where there was collaborative preparatory work, submitting substantially the same final version of any material as another student.

Encouraging or assisting another person to commit plagiarism is a form of improper collusion and may attract the same penalties which apply to plagiarism. Opportunities and temptations for plagiarism have increased with the spread of internet access. Plagiarism is a serious threat to the teaching and accreditation process, and seriously undermines the collegial and ethical principles which underpin the work of a University.

**The Dangers of Plagiarism and How to Avoid It**

The integrity of learning and scholarship depends on a code of conduct governing good practice and acceptable academic behaviour. One of the most important elements of good practice involves acknowledging carefully the people whose ideas we have used, borrowed, or developed. All students and scholars are bound by these rules because all scholarly work depends in one way or another on the work of others.

Therefore, there is nothing wrong in a student using the work of others as a basis for their own work, nor is it evidence of inadequacy on the student's part, provided they do not attempt to pass off someone else's work as their own.

To maintain good academic practice, so that a student may be given credit for their own efforts, and so that their own contribution can be properly appreciated and evaluated, they should acknowledge their sources and they should ALWAYS:
i) state clearly in the appropriate form where they found the material on which they have based their work,
ii) acknowledge the people whose concepts, experiments, or results they have extracted, developed, or summarised, even if they put these ideas into their own words;
iii) avoid excessive copying of passages by another author, even where the source is acknowledged. Find another form of words to show that the student has thought about the material and understood it, but stating clearly where they found the ideas.

If a student uses the work of another person without clearly stating or acknowledging their source, the result is falsely claiming that material as their own work and committing an act of PLAGIARISM. This is a very serious violation of good practice and an offence for which a student will be penalised.

A STUDENT WILL BE GUILTY OF PLAGIARISM if they do any of the following in an assignment, or in any piece of work which is to be assessed, without clearly acknowledging their source(s) for each quotation or piece of borrowed material:

i) copy out part(s) of any document or audio-visual material, including computer-based material;
ii) use or extract someone else's concepts or experimental results or conclusions, even if they put them in their own words;
iii) copy out or take ideas from the work of another student, even if they put the
### Schedule of topics

<table>
<thead>
<tr>
<th>Week No</th>
<th>Week Commencing</th>
<th>Topic</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>1 March</td>
<td>Introduction to audit and assurance services and the auditing profession</td>
</tr>
<tr>
<td>2</td>
<td>8 March</td>
<td>Ethics</td>
</tr>
<tr>
<td>3</td>
<td>15 March</td>
<td>Legal responsibilities</td>
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<tr>
<td></td>
<td></td>
<td><em>(Video: The Auditor in Court)</em></td>
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<tr>
<td>4</td>
<td>22 March</td>
<td>Elements of the financial reporting audit process</td>
</tr>
<tr>
<td>5</td>
<td>29 March</td>
<td>Knowledge of the business and evaluating strategic business risk</td>
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<td><em>(Video: How to Detect and Prevent Financial Statement Fraud)</em></td>
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<tr>
<td>6</td>
<td>5 April</td>
<td><em>No lectures or tutorials this week (Good Friday)</em></td>
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<tr>
<td>7</td>
<td>26 April</td>
<td>Inherent risk assessment and materiality</td>
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<td><em>(Video: 4 Corners – HIH Report)</em></td>
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<td></td>
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<td><strong>MID TERM EXAM Saturday 1 May</strong></td>
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<tr>
<td>8</td>
<td>3 May</td>
<td>Internal control structure and assessing control risk</td>
</tr>
<tr>
<td>9</td>
<td>10 May</td>
<td>Tests of Controls</td>
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<tr>
<td>10</td>
<td>17 May</td>
<td>Substantive tests of transactions and balances</td>
</tr>
<tr>
<td>11</td>
<td>24 May</td>
<td>Completing the audit/Opinion formulation</td>
</tr>
<tr>
<td>12</td>
<td>31 May</td>
<td>Assurance services and Internal Auditing</td>
</tr>
<tr>
<td>13</td>
<td>7 June</td>
<td>Revision</td>
</tr>
</tbody>
</table>
Lecture 3
Legal responsibilities

Video:

*The Auditor in Court* (see page 10 of unit outline for questions relevant to the video)

References:

Gay and Simnett Chapters 4

AUS 210 Irregularities, Including Frauds, and Other Illegal Acts and Errors
AGS 1014 Privity Letter Requests

Tutorial Questions:

4.17, 4.18, 4.25, 4.28, 4.30

Lecture 4
Elements of the Financial Reporting Audit Process

References:

Gay and Simnett Chapter 5

AUS 208: Documentation
AUS 402: Risk Assessments and Internal Controls
AUS 502: Audit Evidence

Tutorial Questions:

5.17, 5.22, 5.24, 5.26, 5.30
Lecture 5
Knowledge of the Business and Evaluating Strategic Business Risk

Video:
How to Detect and Prevent Financial Statement Fraud (see pages 12-15 of the unit outline for material related to the video)

References:
Gay and Simnett Chapter 6
AUS 204: Terms of Audit Engagement
AUS 206: Quality Control for Audit Work
AUS 302: Planning
AUS 304: Knowledge of the Business
AUS 510: Initial Engagement – Opening Balances
AUS 512: Analytical Procedures

Tutorial Questions:
6.16, 6.21, 6.26, 6.29
Prior to Lecture 6 read the case study material on HIH on the text web page http://highered.mcgraw-hill.com/sites/0074711709/student_view0/case_studies.html

Lecture 6
Audit Strategy

Video:
HIH Report – Odds on to Fail

References:
Please read the following material on the HIH case prior to watching the video http://highered.mcgraw-hill.com/sites/0074711709/student_view0/case_studies.html

Gay and Simnett Chapter 7
AUS 302 Planning
AUS 306: Materiality
AUS 402: Risk Assessment and internal controls
AUS 502: Audit Evidence
AUS 708: Going Concern

Tutorial Questions:
7.13, 7.14, 7.19, 7.22, 7.25
This same individual questioned Main Hurdman's ability to objectively audit an inventory system that it had effectively developed. Main Hurdman's independence was also questioned because many of Crazy Eddie's accountants were former members of that accounting firm. Critics charge that a company that hires one or more of its former auditors can more easily conceal fraudulent activities during the course of subsequent audits. That is, a former auditor may help his or her new employer undermine subsequent audits. Crazy Eddie's hiring of several of its former auditors was not unusual; auditors often accept positions with former clients when they leave public accounting. Many accounting firms actually arrange such "placements," a practice that has been widely challenged.

You would think that if an auditor wanted to leave a public accounting firm, he or she would be discouraged from going to work for clients they had audited. Instead, just the opposite is true with big accounting firms encouraging their personnel to work for clients in the apparent belief that it helps cement the accountant-client relationship. 6

Most of the criticism directed at Crazy Eddie's auditors stemmed from their failure to uncover the huge overstatement of the company's inventory and the related understatement of accounts payable. Third parties who filed suit against the auditors charged them with "aiding and abetting" the fraud by failing to thoroughly investigate numerous suspicious circumstances they discovered. Of particular concern were several reported instances in which the auditors requested client documents, only to be told that those documents had been lost or inadvertently destroyed.

In Peat Marwick and Main Hurdman's defense, Antar and his associates engaged in a large-scale plan to deceive the auditors. For example, after discovering which inventory sites the auditors would be visiting at year-end, Antar would ship sufficient inventory to those stores or warehouses to conceal any shortages. Likewise, Crazy Eddie personnel systematically destroyed incriminating documents to conceal inventory shortages from the auditors. Antar also ordered his employees to stop using the sophisticated, computer-based inventory system designed by Main Hurdman. Instead, the accounting personnel were required to return to an archaic manual inventory system previously used by the company. The absence of a computer-based inventory system made it much more difficult for the auditors to determine exactly how much inventory the firm had at any point in time.

A particularly disturbing aspect of the Crazy Eddie scandal was the involvement of several key accounting employees in the various fraudulent schemes. Among the parties who were charged with participating in the fraud or being aware of it were the director of the internal audit staff, the acting controller, and the director of accounts payable. Past experience has proven that a fraud involving the collusion of numerous client executives, particularly key accounting personnel, is extremely difficult for auditors to uncover.

6. Ibid., 42.
- Contact customers
- Interview vendors to confirm returns

4) **Concealment of Liabilities and Expense**
   (a) Fail to record liabilities
   Conceal liabilities (in a draw)

   **Steps to detect**
   - Search for unrecorded liabilities
   - Examine payment after balance sheet date
   - Interview suppliers
   - Examine draws
   - Interview employees

   (b) Record Expense as an asset

   **Steps to detect**
   - Ensure adequate classifications

5) **Improper Valuation of Asset**
   (a) Inventory
   eg: False inventory counts

   **Steps to detect**
   - Unit price reasonable - check invoice price
   - Check alteration of price / counts
   - Compare prior years
   - Be alert! Care with work papers

   (b) Accounts Receivable

   **Steps to detect**
   - Look for unusual transactions
   - Look customers up in the phone book

   (c) Fixed Assets (overvalue assets)

   **Steps to detect**
   Detection of capitalized Expense
   - Examine source documents
   - Check classification - particularly S/T → L/T
   - Interview

6) **Improper Disclosures**
   - Liability omission eg: warranties contingency
   - Related Party transactions
   - Change in accounting policy

   **Steps to detect**
   - Require personal financial disclosures from management
Lecture 9
Substantive Tests of Transactions and Balances

References:
Gay and Simnett Chapter 10
AUS 502: Audit Evidence
AUS 504: External Confirmation.
AUS 506: Existence and Valuation of Inventory
AGS 1002: Bank Confirmation Requests

Tutorial Questions:
10.18, 10.23, 10.32, 10.34

Lecture 10
Completing the audit – Opinion Formulation

References:
Gay and Simnett Chapter 12 and 13
AUS 520 Management Representations
AUS 702 The Audit Report on a General Purpose Financial report
AUS 706 Subsequent Events
AUS 708 Going Concern

Tutorial Questions:

Lecture 11
Other Assurance Services and Internal Auditing

References:
Gay and Simnett Chapter 14 and 15

Tutorial Questions:
14.26, 14.28, 15.15, 15.20