Using Public Company Filings to Plan the Audit and Perform Risk Assessment Procedures

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SUMMARY: This project gives student groups the opportunity to research and analyze publicly available information in the context of audit planning and risk assessment for a publicly traded company. Students simulate an audit team environment and deliver a summary audit-planning memo, risk assessment analytical procedures, and a video presentation in which each audit team presents its findings to the “audit partner.” This project accomplishes several important learning objectives, including (1) familiarizing students with the SEC’s EDGAR database and other public sources of company data; (2) fostering students’ research and critical-thinking skills; and (3) improving students’ understanding of the risk assessment process. This project uses free, publicly available information to achieve these objectives, and the project can be easily modified for subsequent classes by requiring students to utilize the most recent year’s filings when completing the project. The project is appropriate for undergraduate or graduate auditing students.

Keywords: risk assessment; audit planning; analytical procedures; materiality; EDGAR database.

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Supplemental material can be accessed by clicking the link in Appendix B.

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I. INTRODUCTION

Practitioners have embraced the concept of “risk-based auditing” since the 1990s (Weil 2004; Bell, Peccher and Solomon 2005; Knechel 2007; Kachelmeier, Majors, and Williamson 2014), yet the risk assessment process is one of the most frequently occurring areas that have deficiencies in Public Company Accounting Oversight Board (PCAOB) inspections.\(^1\) PCAOB Auditing Standard (AS) 2101.05, *Audit Planning*, states, “Planning the audit includes establishing the overall audit strategy for the engagement and developing an audit plan, which includes, in particular, planned risk assessment procedures and planned responses to the risks of material misstatement” (PCAOB 2010b). Research shows that students can begin to develop risk assessment skills before graduation (Hawkins, Keune, and Saunders 2018). Honing this skill can significantly improve a young professional’s competence and quality of contribution to the audit team.

This project allows audit students to replicate a real-world experience at a public accounting firm, in which an audit team must work together to explore public sources of information about an audit client and use the relevant information to assess risk and plan the upcoming audit of a public company. This project is designed to complement an instructor’s current curriculum and gives students the opportunity to practice critical-thinking skills normally used in the planning stages of an audit, including calculating materiality, identifying significant accounts, identifying and planning responses to fraud risks, and assessing the risk of material misstatement for significant accounts and relevant assertions. It is crucial for today’s accounting students to have a holistic view of the audit-planning and risk assessment process, and we are not aware of any other cases from prior literature that offer students a comprehensive project to practice these skills. The project provides structure similar to the real-world (i.e., where auditors would have audit firm workpaper templates), while leaving enough discretion to foster students’ critical-thinking and problem-solving skills. This opportunity for increasing students’ critical-thinking skills and analytical skills addresses calls from the AACSB (2018) regarding curriculum content guidance.

Each student audit team will choose a publicly traded company, explore the company’s most recent filings in the U.S. Securities and Exchange Commission’s (SEC) Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system,\(^2\) and identify other relevant sources of publicly available information to complete the risk assessment process. Case materials include an in-class activity to help students learn about the different types of filings in EDGAR and the portions of the filings that may be relevant in the risk assessment process. These experiences build upon previous cases that help students explore specific disclosures, such as nonfinancial measures in a 10-K (Hoag and Saucedo 2018), auditor change in an 8-K (Hansen 2017), or audit opinion types in a 10-Q or 10-K (Fay and Stein 2016), by asking students to explore a variety of different filing types and use critical-thinking skills to decide which disclosures are or are not relevant to the audit risk assessment process.

The project was designed with several specific pedagogical goals in mind. First, by choosing their own public company as a research target, students engage with the material more deeply, which improves learning (e.g., Biggs 1989). Real-world examples help students understand complex principles and engage with abstract theories like audit risk assessment (Tucker 2017).

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\(^1\) “The most frequently identified audit deficiencies continue to persist in similar areas across firms: assessing and responding to risks of material misstatement; auditing internal control over financial reporting; and auditing accounting estimates, including fair value measurements” (Franzel 2017).

\(^2\) https://www.sec.gov/edgar/searchedgar/companysearch.html
Second, working in cooperative teams helps students develop critical soft skills (e.g., Tarricone and Luca 2002) in an integrated way (e.g., Montano, Donoso, Hassall, and Joyce 2010). Students in cooperative learning environments (i.e., teams) offer more positive feedback on satisfaction, perceived learning, and effectiveness of the method (Riley and Ward 2017). Third, introducing students to current technology like the EDGAR database and XBRL improves their financial literacy and ability to read and interpret financial statements (e.g., Debreceny and Farewell 2010). Finally, this project constitutes a deep learning experience whereby students gain a greater understanding of the material that they have learned in class by applying it to a specific company, rather than reproducing information in other forms of assessments like quizzes and exams. Prior research demonstrates that similar deep learning activities improve student performance and retention (e.g., Everaert, Opdecam, and Maussen 2017; Hansen 2017).

This project is appropriate for undergraduate or graduate auditing students. Importantly, because the project requires students to use publicly available information, the case can be reused year after year as companies release updated quarterly and annual financial statements. Instructors can customize the assignment to match the normal course content by removing or adding specific components (e.g., establishing materiality, designing audit procedures). The next section presents the case as conducted at a large public university. The “Case Learning Objectives and Implementation Guidance” section presents the learning objectives, evidence of case efficacy using anonymous student survey responses, and an optional activity that can be used to familiarize students with EDGAR filings. The Teaching Notes contain a sample grading rubric and solutions to the optional EDGAR filing activity, along with example submissions. Because the case requires that students pick different public companies, and because the risk assessment process requires significant judgment, there is no “solution” to the case. Instead, instructors can evaluate student performance relative to the normal course instruction of the related topics.

**II. THE CASE**

Your audit firm, VoLS LLP, recently gained a new public client. The partner has assigned your team to do the fieldwork for this audit and has asked you to do a preliminary risk assessment. You do not yet have any prior year workpapers from the predecessor auditor, so your partner is interested in seeing how much you can learn based strictly on publicly available information. Specifically, she wants you to obtain an understanding of the company and its environment, identify the significant accounts and disclosures, and, for each of those, do a preliminary assessment of the risk of material misstatement for each relevant assertion. She expects your consideration of risk of material misstatement to be whether that risk is due to error or fraud, and to identify potential fraud risks that could be discussed in the upcoming team fraud-brainstorming session (i.e., potential opportunities and incentives/pressures to commit material fraud in the company). She expects that your analysis will include both qualitative factors and quantitative factors based on risk assessment analytical procedures. Since you have not started fieldwork yet, you will not be able to do a preliminary assessment for control risk. Thus, as it relates to control risk, your only responsibility will be to determine whether there were any material weaknesses in the prior year that you should consider in the upcoming year’s audit.

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3 The case was originally designed for, and efficacy-tested in, undergraduate audit classes. However, it could be modified for graduate audit classes by increasing expectations on the length and quality of the required deliverables.
Because this is a publicly traded company, she informs you that the planning procedures for
the audit should comply with auditing standards set forth by the Public Company Accounting
Oversight Board (PCAOB):

- AS 1101: Audit Risk (PCAOB 2010a);
- AS 2101: Audit Planning (PCAOB 2010b);
- AS 2105: Consideration of Materiality in Planning and Performing an Audit (PCAOB 2010c);
- AS 2110: Identifying and Assessing Risks of Material Misstatement (PCAOB 2010d).

She has noted the following resources to help you with your search of information commonly
available for public clients. She would like you to consider each of these sources and think
carefully about how the information you learn relates back to the risk of material misstatement in
the audit.

- **Form 10-K (EDGAR):** annually filed financial statements and other important information for
  shareholders. Be careful using “risk factors” (Item 1A) because these are written from the
  perspective of the shareholder or a potential investor. Typically, auditors can determine
  what affects the risk of material misstatement by reading Business, Management’s
  Discussion and Analysis, Critical Accounting Policies and Estimates, discussion of any
  pending or threatened litigation or other contingencies, the Financial Statements, and the
  Notes to the Financial Statements.

- **Form 10-Q (EDGAR):** quarterly filed financial statements and other important information
  for shareholders. The 10-Q should always be read in conjunction with the most recently filed
  10-K because disclosures are limited to material changes since the last 10-K.

- **Form 8-K (EDGAR):** periodic filings that report material events or transactions throughout
  the year. Pay particular attention to these items:
  - Items 1.01 and 1.02: Entry/termination from a material agreement;
  - Item 1.03: Bankruptcy or receivership;
  - Item 2.01: Acquisition/disposition of assets;
  - Item 2.02: Results of operations and financial conditions;
    - You should also consider listening to a webcast or reading a transcript from the
      earnings conference call (typically on the Investor Relations website).

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4 PCAOB Auditing Standards are available at https://pcaobus.org/Standards/Auditing/Pages/default.aspx. It is
not necessary to read these standards to complete the case. However, it is important for students to understand
the source of the standards that guide audit firms’ planning processes. These standards relate closely to the
planning and risk assessment chapters of commonly used auditing textbooks in the U.S.: Chapters 8–10 in
Arens, Elder, Beasley, and Hogan (2017), Chapter 7 in Johnstone, Gramling, and Rittenberg (2016), Chapters
3 and 4 in Louwers, Blay, Sinason, Strawser, and Thibodeau (2018), Chapters 3 and 4 in Messier, Glover, and
Prawitt (2019), and Chapter 6 in Whittington and Pany (2019).

5 A full list of 8-K topics is available here: https://www.sec.gov/fast-answers/answersform8khtm.html

6 What are investors asking about? How does management characterize this year’s performance? Do there
appear to be any major pressures or incentives on management? Remember that companies are required to
report GAAP EPS (the EPS you learn in class), but they can also report Non-GAAP EPS if they believe that
GAAP EPS is misleading or not representative of “core” performance. Some companies have been abusing
these Non-GAAP adjustments in a way that the auditor should think about when brainstorming pressures and
incentives on management (Guske 2015; Trainer 2016; Golden 2017; SEC 2018).
These filings often contain management forecasts. You should also consider analyst forecasts that will be available from other sources, including Yahoo! Finance and https://new.nasdaq.com/.\(^7\)

- **Items 2.03 and 2.04:** Material changes in financial obligations and off-balance sheet arrangements;
- **Items 2.05 and 2.06:** Material impairments or costs associated with exit activities;
- **Item 4.01:** Change of auditors reported;
- **Item 4.02:** Announcement of a restatement (non-reliance);
- **Items 5.01 or 5.02:** Changes in ownership, directors, or management;
- **Items 5.07 or 5.08:** Shareholder voting;
- **Item 7.01:** Regulation FD disclosure;
- **Item 8.01:** Other material events; and
- **Item 9.01:** Financial statements and exhibits.

- **DEF 14A (EDGAR):** annually filed proxy statement containing information that is relevant to shareholders for voting in annual meetings. This includes information about the board of directors and executive compensation.

- **UPLOAD or CORRESP (EDGAR):** The SEC periodically reviews the 10-K and other related filings to determine compliance with GAAP and other SEC disclosure requirements. The SEC issues their comments in a letter to the company, filed as an UPLOAD filing. The company then responds to those comments by providing clarification, promising to improve disclosure in the future, or agreeing to restate previously filed information. The company’s responses are filed as a CORRESP filing.

- **Investor Relations website:** typically available as a separate website from the company’s customer-facing website and contains many of the filings above, plus other information in a more user-friendly interface.

The partner wants you to think carefully about all of the information learned from the sources above, identify the information that is relevant to assessing the risk of material misstatement, conduct risk assessment analytical procedures, and then summarize your final conclusions in an audit-planning memo that is written professionally and free of grammatical or typographical errors such that it could be included in the audit workpapers. To help you organize your thoughts, the partner recommends following this outline for the memo:

1. Background information about the company that is relevant to the audit.
2. Identification of financial-statement-level risks of material misstatement (consider factors such as geographic locations, complexity of operations, litigation risk, industry, operating segments, management and director backgrounds, etc.). Be sure to explain how any financial-statement-level risks you identify relate to the risk of material misstatement in your upcoming audit.
3. Calculation of overall financial statement materiality and tolerable misstatement.
   a. Since you are planning the upcoming audit, think about the net income, revenues, and assets from the most recent 10-K, and then consider whether there have been any signs of material changes for the upcoming audit based on subsequently filed 10-Qs or management forecasts.

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\(^7\) You can learn more about earnings forecasts here: [https://www.investopedia.com/articles/stocks/06/earningsforecasts.asp](https://www.investopedia.com/articles/stocks/06/earningsforecasts.asp)
4. Identification of “significant” (in-scope) accounts and disclosures (feel free to use an appendix or reference a chart). Remember to consider both qualitative and quantitative factors when determining significant accounts.

5. Results of the risk assessment analytical procedures.

6. Identification of potential fraud risks that should be considered in the team fraud brainstorming session.
   a. Pressures/incentives to commit fraud (whether through GAAP or non-GAAP metrics, management’s concerns with analyst forecasts, executive compensation benchmarks, cash versus stock-based compensation, etc.).
   b. Opportunities to commit fraud (consider prior-year internal control material weaknesses, accounts, and disclosures requiring significant estimates or judgment, etc.).

7. Recommendations for the preliminary assessment of the risk of material misstatement for each significant account and relevant assertion.
   a. This should be based on all the information described above and could be presented in tabular format similar to that shown below. Feel free to use qualitative assessments such as “High” “Medium” or “Low.”8 This should be done for every significant account and every relevant assertion. If you think that the risk of a certain assertion is so low for a specific account that it does not need to be tested, then you can consider that assertion as not relevant to the account. You can use the planning memo or the planning meeting video to justify any difficult decisions. Please assume that the audit partner has set audit risk at “Low” as you make your decisions:

| Account | Assertion | RMM | Detection Risk |
|---------|-----------|-----|----------------|
| Cash    | Existence |     |                |
| Cash    | Valuation |     |                |

8. Select five of the highest-risk account/assertion combinations and describe some potential substantive auditing procedures that could be conducted to address the risk.

9. Other information or issues identified, but not mentioned previously, that the partner should consider when planning the audit.

The partner would then like to do a quick video conference with you to hear you summarize the most important issues from the memo in a 10–15 minute presentation. You can assume that the partner has read your audit-planning memo when you conduct the presentation.

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**Project Requirements**

1. Pick a publicly traded company and receive approval from your instructor before proceeding. You should choose a company whose operations you are already generally familiar with, preferably one that operates in a single industry with a single product line, such as The Columbia Sportswear Company, Home Depot, Marriott International, Netflix, Inc., Southwest Airlines Co., or Target Corporation.

2. Turn in a single-spaced, audit-planning memo, no longer than ten pages, that includes headings to separate the various sections recommended by the partner and a reference

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8 Note that these are only recommended classifications and may vary with audit firm policy. PCAOB Auditing Standards emphasize the identification of “significant risks,” which might be comparable to the “High” category used on this project. Your instructor may provide alternative instructions that align with the course textbook.
page of the various information sources used to complete the audit-planning memo. Feel free to use bullets and tables to visually organize lists.

3. Turn in your risk assessment analytical procedures (in Excel, with formulas so that your instructor can see how you calculated changes, ratios, etc.). Ensure that each procedure is clearly labeled (e.g., “% Changes 2017 versus 2018” or “Five-Year Trend of Ratio A”) in a way that can be referenced to the conclusions and discussions in the memo.

4. Record a 10–15 minute video and upload it to YouTube, using the “unlisted” feature, to ensure privacy. Your instructor will not share this video with anyone else.

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III. CASE LEARNING OBJECTIVES AND IMPLEMENTATION GUIDANCE

Learning Objectives

The learning objectives (LOs) of this project were identified to help bridge the gap between theory and practice, based on experience in teaching theoretical audit concepts, discussions with students returning from internships and first-year employment, and discussions with current practitioners, including audit managers and audit partners. Specifically, the LOs are as follows:

- **LO1**: Provide an opportunity for students to use critical-thinking skills.
- **LO2**: Increase students' understanding of the use of SEC filings and other publicly available information in the planning risk assessment process for an external audit.
- **LO3**: Increase students' understanding of how to calculate materiality and identify significant accounts.
- **LO4**: Increase students' understanding of performing risk assessment analytical procedures in the planning risk assessment.
- **LO5**: Increase students' understanding of identifying the most relevant management assertions and provide an opportunity for students to design audit procedures to address the risk of material misstatement for specific account-assertions.
- **LO6**: Improve students' understanding of how to perform a planning risk assessment for an external audit based on publicly available information.
- **LO7**: Improve students' ability to identify and synthesize relevant information through written and verbal communications.
- **LO8**: Increase students' confidence in conducting and presenting a realistic audit plan for actual clients.

Implementation Guidance

The case is designed to be an out-of-classroom experience whereby students apply the concepts from the current curriculum to a real company purported to be a fictional client. The instructor used one class period to introduce the project. Students worked on the project over the course of multiple weeks outside the classroom, and the instructor answered student questions during regularly scheduled office hours.

While this project attempts to provide a real-world experience for audit risk assessment, documentation in a memo may not mirror the practices that students will experience in the field. Many audit firms have tailored electronic workpaper systems to capture the planning process in different formats (e.g., Excel spreadsheets, customized user interfaces). Instructors should inform students about current practices in workpaper documentation when assigning the project, recognizing that in the absence of proprietary audit documentation software, this project allows students to document the same content and conclusions that would be captured in other formats.9

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9 Instructors can utilize alumni and recruiter contacts to discuss current workpaper practices. Other available sources include Messier et al. (2019) Earthwear workpaper templates (available at: http://highered.mheducation.com/sites/1259969444/student_view0/earthwear.html), the EY Academic Resource Center (available at: https://www.ey.com/us/arc), and the Deloitte Trueblood Case Studies (available at: https://www2.deloitte.com/us/en/pages/about-deloitte/articles/trueblood-case-studies-deloitte-foundation.html).
Instructors should encourage students to pick a public company in which they are interested and generally familiar with that company’s business operations. Their interest can stem from being familiar with the company’s products, interest in future employment at the company, or interest in providing audit services or other professional services to the company. Instructors can also encourage students to pick companies that operate in industries that align with future career goals. Our experience in teaching the case suggests that operations related to retail, manufacturing, or services are easiest for the students to follow. We recommend that students avoid companies in banking, financial services, medical, technology, or utilities unless they have prior experience in the industry, class time has been devoted to it, or they have a special interest in that type of company. The instructor should emphasize to the class that students should first verify that their company is a U.S. publicly traded company (with a ticker symbol listed on a U.S. stock exchange).

Before assigning this project, instructors used one class period to help students gain confidence in navigating the EDGAR database. As a pre-class ungraded assignment, students completed the handout shown in Appendix A for a publicly traded company not assigned to any of the groups as of the date of class (in Appendix A, Southwest Airlines is used to be consistent with the student example provided in the Teaching Notes). In class, instructors then walked through the assignment and answered questions for which students had difficulty finding the information on their own. Using the SEC’s EDGAR database may be overwhelming for students if they have had very limited experience using EDGAR in other accounting classes. In the Teaching Notes, we provide a sample solution to the Appendix A assignment for instructors who may not be familiar with the EDGAR database.

Instructors also spent time in class discussing management forecasts and analyst forecasts and completing a risk assessment analytic. This exercise provided students with a baseline expectation for risk assessment analytics in the group assignment. Instructors limited the expectation to a vertical analysis (i.e., evaluating each account as a percent of total assets or total revenues), a horizontal flux analysis (i.e., dollar and percent changes in account balances between periods), and ratio analyses over three years. Instructors can adjust course expectations for the thoroughness and complexity of risk assessment analytics based on other course objectives. Before assigning this project, the instructor can demonstrate management forecasts available on a company’s investor relations website and analyst forecasts available online (e.g., Nasdaq.com [https://www.nasdaq.com/] or Yahoo! Finance [https://finance.yahoo.com/]). Instructors may also wish to explain how prior quarterly earnings and seasonally adjusted earnings are also benchmarks that set the stage for management’s expectations of earnings and how this might fit into their audit plan.

Instructors used the YouTube unlisted video feature to avoid spending in-class time on group presentations. Instructors provided students with resources in the library to troubleshoot technical problems with recording and uploading. Instructors emphasized that the video would be graded for content and professionalism only, and not for video-editing skills, since video editing is not one of the learning objectives of the course or the project. Many student groups submitted videos recorded through Zoom (https://zoom.us/) or using the camera feature on a smartphone.

In a full semester, students were allowed approximately six weeks between the date of assignment and due date. In a condensed summer term, students were allowed approximately two weeks between the date of assignment and due date. There was no noticeable difference in student project quality, which suggests that either timeframe provides adequate time for students to complete the project. Instructors may discourage students from using previous sections’ work by instituting a policy that disallows a recently selected company to be chosen again. Instructors
teaching multiple sections can institute a policy that disallows the same company being chosen across sections.

While the group element of the project simulates real-world audit teams, an inevitable issue of group work is the “free rider” problem. When distributing the project, instructors encouraged teams to begin meeting immediately and to avoid “dividing up the work” since risk assessment should be a holistic process. Instructors then communicated the following message when introducing the project:

You are encouraged to begin your group work early so that you can identify any potential “free rider” problems. If a free rider problem emerges, please contact the instructor immediately so that the non-contributing team member may be assigned a new company to complete as an individual project. Because risk assessment requires a holistic view of the company, you should not divide up the work between team members. If the instructor suspects that work was divided, the instructor reserves the right to separately interview each team member and adjust the group and individual grades accordingly.

Students were given written feedback using the grading rubric provided in the Teaching Notes.

Evidence of Efficacy

We tested efficacy of the project using student perceptions of whether the project achieved LO1–LO8. Data were collected across two different instructors; group sizes averaged three to five students. To ensure that students would be able to differentiate the perceptions of the project from perceptions of normally scheduled lectures of the related material, instructors assigned the project as a capstone project after completion of the midterm exam. The midterm exam was a multiple-choice assessment that covered the majority of the topics included in the project, such as planning, materiality, the risk assessment process, and SEC filings relevant to the audit.10 The instructors conducted a pre-project survey to determine students’ baseline knowledge of risk assessment and SEC filings. Because the pre-project survey was issued immediately following the midterm exam, we expected students to report that they had at least some knowledge of each of the areas covered in the project. The instructors then conducted a post-project survey to directly assess LO1–LO8.11 All post-project survey questions were on a five-point scale, with 1 indicating strongly disagree, 3 indicating neutral, and 5 indicating strongly agree. The results of the survey are shown in Table 1. A total of 92 students completed the pre-project survey and 90 students completed the post-project survey. This represents a response rate greater than 96 percent based on 94 enrolled students across two instructors.12 Students report spending, on average, 12 hours working on the project.

As reported in Table 1, Panel A, the pre-survey results of 3.0 or higher demonstrate that students already feel that they have at least “some” knowledge of the following areas: knowledge of SEC filings used by auditors, knowledge of materiality, and knowledge of assertions and procedures (mean of 2.98 is not statistically different from 3.0). The only area for which students report at least “some” comfort in the pre-survey relates to calculating materiality and significant accounts. This is, perhaps, not surprising given the general simplicity of the calculation. The lower

10 Students do not necessarily need a prior understanding of the EDGAR website or the filings as the project facilitates learning more about the SEC filings.

11 This post-project, self-assessment form of efficacy is similar to the questions used in Fay and Stein (2016) and Hansen (2017), modified for our learning objectives.

12 We noted no significant differences across instructors.
The comfort scores for the remaining areas suggest that classroom lectures and exam-form assessments may not be sufficient to help students feel comfortable in executing some of the more theoretical areas of an audit such as risk assessment, assertions, and designing audit procedures. The low scores on knowledge and comfort related to performing analytical procedures support the AACSB’s (2018) call for more classroom integration of data analytics. Finally, students report at least “some” interest in the topic of the case, using SEC filings and other publicly available information to plan the risk assessment process.

The post-survey results, reported in Table 1, Panel B, indicate that the project was effective in meeting all the learning objectives. All questions have a response mean that is statistically greater than the “neutral” response of “3” (p < 0.01) and the median is “agree” (“4”) for all questions. This is encouraging because it suggests that the project is effective for the intended comprehensive purpose of raising student knowledge, and confidence for more than just one area of audit competence. While we did not perform rank-order analyses, anecdotally based on the means, the group project was most effective for achieving LO1 (use critical thinking) and LO2 (improving understanding of SEC filings and other public information in risk assessment). Despite pre-survey

### TABLE 1
Student Feedback

Panel A: Pre-Project Questionnaire (n = 92)

| Question                                                                 | Mean  | Median | Std. Dev. |
|------------------------------------------------------------------------|-------|--------|-----------|
| Rate your knowledge of SEC filings and other publicly available information that could be used by an external auditor in the planning risk assessment process. | 3.054 | 3.000  | 0.717     |
| Rate your knowledge of calculating materiality and identifying significant accounts. | 3.685 | 4.000  | 0.769     |
| Rate your knowledge of performing analytical procedures in the planning risk assessment. | 2.826 | 3.000  | 0.779     |
| Rate your knowledge of identifying relevant management assertions and designing audit procedures to address the risk of material misstatement for a specific account-assertion. | 2.978 | 3.000  | 0.812     |
| How comfortable are you using SEC filings and other publicly available information in the planning risk assessment process for an external audit? | 2.826 | 3.000  | 0.921     |
| How comfortable are you calculating materiality and identifying significant accounts? | 3.663 | 4.000  | 0.816     |
| How comfortable are you performing analytical procedures in the planning risk assessment? | 2.620 | 3.000  | 0.796     |
| How comfortable are you identifying relevant management assertions and designing audit procedures to address the risk of material misstatement for a specific account-assertion? | 2.826 | 3.000  | 0.885     |
| How interested are you in the topic of using SEC filings and other publicly available information in the planning risk assessment process for the external audit? | 3.250 | 3.000  | 1.065     |

Each question in Panel A was asked on a scale of 1 to 5, where 1 = no knowledge (comfort, interest), 3 = some knowledge (comfort, interest), and 5 = high knowledge (comfort, interest).

(continued on next page)
results of higher knowledge and comfort regarding calculating materiality, the group project was still able to improve students’ understanding of the process.

We also asked students to provide qualitative feedback for the following two statements: “Please describe what you liked about the group project” and “Please describe what you would recommend to improve the group project.” Common themes in the responses suggest that students valued the real-world applicability of the project. The majority of responses noted that the project helped put various audit concepts and planning activities into greater perspective and gave them increased confidence in executing similar tasks at their future jobs. Many students also stated that the group aspect of the project was very useful, as it helped them better collaborate and

| Question                                                                 | Mean     | Median | Std. Dev. |
|---------------------------------------------------------------------------|----------|--------|-----------|
| LO1: The group project required me to use critical-thinking skills.       | 4.378*** | 4.000  | 0.712     |
| LO2: The group project improved my understanding of the use of SEC filings and other publicly available information in the planning risk assessment process for an external audit. | 4.367*** | 4.000  | 0.771     |
| LO3: The group project improved my understanding of calculating materiality and identifying significant accounts. | 4.200*** | 4.000  | 0.950     |
| LO4: The group project improved my understanding of performing analytical procedures in the planning risk assessment. | 4.089*** | 4.000  | 0.920     |
| LO5: The group project improved my understanding of identifying relevant management assertions and designing audit procedures to address the risk of material misstatement for a specific account-assertion. | 4.067*** | 4.000  | 0.939     |
| LO6: The group project improved my understanding of how to perform a planning risk assessment for an external audit based on publicly available information. | 4.222*** | 4.000  | 0.832     |
| LO7: The group project improved my ability to identify and synthesize relevant information through written and verbal communications. | 4.044*** | 4.000  | 0.847     |
| LO8: The group project improved my confidence for doing similar analyses on actual clients. | 3.956*** | 4.000  | 0.873     |
| I would recommend this group project as a learning tool for future auditing classes. | 4.044*** | 4.000  | 0.947     |
| The instructions and background information in the group project were clear. | 3.844*** | 4.000  | 0.959     |
| The group project was interesting. | 3.787*** | 4.000  | 0.982     |
| The group project was the appropriate level of difficulty for this course. | 4.078*** | 4.000  | 0.915     |
| Total time spent on the project (in hours) | 12.195   | 10.000 | 6.989     |

***, **, * Indicate that the sample mean is statistically different from the “neutral” response of “3” based on a z-statistic with p-value < 0.01, 0.05, and 0.1, respectively (not applicable for the total time question).

Each question in Panel B was asked on a scale of 1 to 5, where 1 = strongly disagree, 3 = neutral, and 5 = strongly agree.
gain an understanding of how audit teams function in the profession. Another common theme on which students commented was the fact that being able to select their company made the project more interesting and enjoyable. Representative examples include:

- “It required me to think more critically and creatively, especially with regards to designing audit procedures. I feel like I understand calculation of materiality and analytical procedures much better.”
- “I really liked that we were able to take what we have learned throughout the semester and put it in a real-life situation of an external audit. I struggled with the material before the project, but I think being able to see it and talk it out helped my understanding a lot.”
- “I liked that this was truly a ‘group’ project. It was not a project that you could just split up to divide and conquer. You really had to communicate and work with everyone because a lot of the issues or problems that evolved with the planning phase had to be talked through extensively. Also, when preparing and shooting the video, I think that really helped prepare a lot of us with organizational skills and time management. I learned that I have to be able to explain what I/we did to a peer and boss and make it understandable.”

Collectively, the quantitative and qualitative evidence leads us to conclude that the project was effective in meeting the learning objectives.13

TEACHING NOTES AND STUDENT VERSION OF THE CASE

Teaching Notes and the Student Version of the Case are available only to non-student-member subscribers to Current Issues in Auditing through the American Accounting Association’s electronic publications system at http://aaapubs.org/. Non-student-member subscribers should use their usernames and passwords for entry into the system where the Teaching Notes can be reviewed and printed. The “Student Version of the Case” is available as a supplemental file that is posted with the Teaching Notes. Please do not make the Teaching Notes available to students or post them on websites.

If you are a non-student-member of AAA with a subscription to Current Issues in Auditing and have any trouble accessing this material, please contact the AAA headquarters office at info@aaahq.org or (941) 921-7747.

REFERENCES

AACSB. 2018. Eligibility Procedures and Accreditation Standards for Accounting Accreditation. Exposure Draft #1, November 6. Available at: https://www.aacsb.edu/-/media/aacsb/docs/accreditation/accounting/standards-and-tables/2018-accounting-standards-ashx?la=en&hash=8DCDA6CE3B0CEF6AB82D39CBF53995DA96111196

Fay, R. G., and S. E. Stein. 2016. Teaching students about audit reports: An interactive approach. Current Issues in Auditing 10 (2): I14–I25. https://doi.org/10.2308/ciia-51410

13 These results were also confirmed by a second assessment (untabulated) for which instructors changed the timing of the project from post-midterm to pre-midterm, in order for students to complete the project outside of class parallel to regular class content. We then compared midterm exam scores between the post-midterm semester and the pre-midterm semester. We found that the average student performance on project-related questions on the midterm increased from 71 percent to 81 percent. In the same exam, average student performance on non-project related questions stayed constant at 72 percent. From this we conclude that the project is more effective in helping students understand and apply class content than from lecture alone.
APPENDIX A

Activity for Familiarizing Students with SEC EDGAR

It is important to understand the different sources of information available to an auditor. The auditor will have access to virtually all information for a company that is relevant to the financial statement audit (or internal control audit). This includes everything from shipping records to vendor invoices to payroll files to board of director minutes. However, auditors only gain access to the private, internal information once they have accepted the engagement and started fieldwork. Before that happens, the auditor should use various sources of public information to (1) decide whether the auditor wants to be affiliated with this client (client acceptance), and (2) perform a preliminary risk assessment based on publicly available information. It is important that the auditor gain this foundational level of understanding about the client’s business, industry, and operations before starting the audit.

Public companies are required to conform to the periodic disclosure requirements set forth by the SEC. Any information that is required to be filed with the SEC will be available on the EDGAR website: https://www.sec.gov/edgar/searchedgar/companysearch.html/.

Using “Southwest Airlines” (ticker LUV) and the EDGAR link above, take some time to explore the various types of filings that are most relevant to an auditor (print or copy this into a Word document and fill in the blanks):

- **10-K filings** provide investors with comprehensive information about the financial condition of the company, internal control quality, and the risks of investment. The audited financial statements are part of the 10-K filing. Companies file one 10-K filing per year.

In the EDGAR Search Results for Southwest Airlines, identify the most recent 10-K filing. You can quickly find this by typing “10-K” into the “filing type” field for filtering results. Once you locate the latest 10-K, click “Documents.”

- What is the Filing Date of this 10-K filing? ____
- What is the fiscal year-end (“Period of Report”)? ____

Next, click the link next to “FORM 10-K.” Once in the filing, identify the most pertinent parts of the filing:

- What is Southwest's filing status (Large Accelerated Filer, Accelerated Filer, Non-Accelerated Filer, and/or Smaller Reporting Company)? ____
- **Item I. Business.** This provides investors with information about the nature of the business for which they are investing.
  - What are Southwest’s segments? ____
  - How many employees? ____
  - What is the CFO’s name, and how long has s/he been in that role? ____

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Item IA. Risk Factors. These risks are important for investors to understand from the perspective of their investment. Identify at least one risk that you think would be of interest to auditors because it could increase the risk of material misstatement of the financial statements.

Item 3. Legal Proceedings. As we will discuss later in the semester, auditors send confirmation letters to the company’s attorney to receive information about the status of any pending or threatened litigation that requires accrual or disclosure in the financial statements.

Item 6. Selected Financial Data.
- Five-Year Financial Summary. Which account appears to have had the biggest changes over the previous five years?

Item 7. Management’s Discussion and Analysis.
- What are some major changes to the operations of the company in the past year?
- For the account you picked from Item 6 above, did management provide an explanation for the major change?
- What metric(s) does the company use to evaluate its performance? (Hint: See “Returns”)
- Contractual Obligations give investors a sense of how much cash will be necessary to pay off the company’s debt and lease payments in the next five years. What is the total amount of commercial commitments due in the future?
- Summary of Critical Accounting Estimates. Familiarize yourself with Southwest’s critical accounting estimates. Which accounting estimates seem to have the largest risk of manipulation by management?

Item 8. Audited Financial Statements.
- What are the pages of the financial statements?
- How many footnotes?
- Which account do you think is the hardest to audit?
- Which account do you think has the highest risk of material misstatement? Why?
- On what page(s) is the auditor’s opinion?

Management’s Report to Shareholders and Management’s Report on Internal Controls.
- Any other issues not previously identified?
- Did management identify any material weaknesses or significant deficiencies?

DEF 14A filing. Shortly after the 10-K filing date, the company will file a DEF 14A. This filing provides important information for shareholders to prepare them for the annual meeting and for shareholder voting. Some areas of particular interest to the auditor include:
- Executive compensation: The portion of an executive’s pay that is fixed does not provide much incentive for fraud (e.g., salary). However, there are “performance-based” or “incentive-based” compensation, or “equity-based” compensation. These vary significantly (think millions of dollars) with the performance of the company. It is important for auditors to understand how management is compensated in order to know whether there are any overly aggressive benchmarks or pay structures that would provide undue influence to commit fraud.
- Board of Director profiles: Profiles for board members are included in the DEF 14A filing. (Some companies also include executive profiles here instead of in the 10-K filing.)
Auditors use background information for executives and board members to determine whether they appear properly qualified for their position.

Locate the latest DEF 14A filing for Southwest.

- Locate the compensation table(s) for the Chief Executive Officer. How much did (s)he get paid in the most recent year? Break it down by type of compensation. ______
- Locate the part of the compensation disclosure that describes how performance/incentive/equity compensation is determined. It should describe certain benchmarks or performance measures used by the company (this is called the “Pay for Performance” disclosure). Describe the way the CEO’s performance/incentive/equity compensation is determined. If you were the auditor, how would this affect your audit? ______
- Locate the profile for the Chair of the Audit Committee. Describe the audit committee chair’s background. Does it appear to involve sufficient financial experience? ______
- Also locate the Audit Committee Charter, or a description of what the audit committee does. Anything of particular interest to you? ______
- Scan through and locate the other types of items being voted on by shareholders. See anything interesting? ______

- **10-Q filings** provide interim information to shareholders between 10-K filings.
  - How many 10-Q filings did Southwest file in the previous 365 days? ______
  - Open the most recent 10-Q filing. Quickly scroll through the filing, along with the financial statements. Do they look different than the 10-K? How? ______

- **8-K filings** provide investors with timely information about material transactions that occur throughout the year. Some companies will have dozens of 8-K filings each year, while other companies have less than a handful. Relevant information to an auditor will be anything that affects the financial statements, such as:
  - **Executive or director turnover**—management and the board of directors are key parts of the internal controls of a company. An auditor will be interested in the professional qualifications of the outgoing and incoming executive or director, and the reason for the change (in case that reveals new risks or uncertainties at the company).
  - **Auditor changes**—the company must disclose to the public, on a timely basis, whenever an auditor has been notified that their services are no longer needed, and when the company appoints a new audit firm. Oftentimes, these things happen at once, but if there is a disagreement between the company and the auditor, the company may first “dismiss” their auditor before engaging a new one. Another reason this may not happen at once is if the auditor “resigns” and the company needs time to find a new one. SEC rules require that the filing states whether the company dismissed the auditor or the auditor resigned, whether there were any disagreements between the auditor and management, and the dates of the change.
  - **Material transactions**—new debt or equity issuances, mergers, acquisitions, dispositions, etc. Any time there is a material transaction, the SEC requires timely notification to shareholders.
  - **Restatements**—if management and the board of directors (usually in coordination with the auditor) determine that previously issued financial statements can no longer be relied upon, they disclose the issue in Item 4.02 of an 8-K filing.

Go back to the search results for Southwest and obtain a list of all 8-K filings issued in the previous 365 days. Use the grid below to fill out all the 8-Ks and then use a website like Yahoo! Finance to determine whether there are any major movements in stock price for LUV around the
same date. Because 8-Ks can be filed a few days after an event, you should look for stock price movement beginning several days before the filing date. If needed, you can add more rows to the grid.

| 8-K Filing Date | Disclosed Information | Was the Auditor Mentioned? | Did the Stock Price Move? |
|-----------------|-----------------------|-----------------------------|---------------------------|
|                 |                       |                             |                           |
|                 |                       |                             |                           |
|                 |                       |                             |                           |
|                 |                       |                             |                           |

Appendix A is available for download, see the link in Appendix B.

APPENDIX B

ciia-52472_Appendix A: http://dx.doi.org/10.2308/ciia-52472.s01