SAS # 99 Consideration of Fraud in a Financial Statement Audit

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Part of the series of Statements on Auditing Standards (SAS), was issued in October 2002 by the AICPA Auditing Standards Board.

The original exposure draft was distributed in February 2002. SAS 99, which supersedes SAS 82, was issued partly in response to recent accounting scandals at Enron, WorldCom, Adelphia, and Tyco.

The standard incorporates recommendations from the Public Company Accounting Oversight Board (PCAOB), and various other contributors including the International Auditing & Assurance Standards Board. SAS 99 became effective for audits of financial statements for periods beginning on or after December 15 2002.
SAS# 99 Requires an assessment of the potential risks

- Brainstorming sessions with stakeholders
- By Auditors and Auditee; But, you also develop a session within the organization: Same objectives:
  - At LISD: CFO, Accounting Director, Senior Accountants, Superintendent; and all administrators are required to go through a review session.

- Objective IS to share their experiences with the client and how a fraud might be perpetrated and concealed.
- Objective IS to set the proper “tone at the top” for conducting the engagement.
- Models the proper degree of professional skepticism and sets the culture for the entire engagement.
The review session in LISD consists of

☐ What are the elements of Fraud?
☐ What is an internal control?
☒ What is Fraud?
Elements of Fraud

☐ 1. Incentive
☐ 2. Opportunity
☐ 3. Rationalize
☐ 4. Potential
What is Fraud?

- Fraud, unlike an error, is intentional and usually involves deliberate concealment of facts
What is an internal control?

- An internal control is a procedure to ascertain a financial asset or to prevent a loss of an asset.
- Qualities of an internal control:
  - Prevention – to bring out problems
  - Detection – to avoid problems
  - Assertion – to account for
Auditor to use information to identify risks that may result in a material misstatement

☐ Risk Assessment:
☐ This section specifically requires that an assessment be made regarding improper revenue recognition and management override of controls be considered.

☐ At LISD, we have two risk assessment models:
   Internal Auditor develops an annual assessment tool for managers to follow.

☐ Also, CFO develops an assessment from the policies perspective and controls to determine if there are areas that may need more training and monitoring.
SAS # 99 Requires auditor to use the information gathered to identify risks that may result in a material misstatement

☐ Requires external auditors to assess whether there is a risk of a potential material misstatement

At LISD, our district provides the auditors with information that they can access via our website: Monthly, the following information is provided to our Board and it is posted on our website.
LISD Monthly Reports

- Monthly Financial Statements
- Monthly Investment Report
- Monthly Tax Report
- Monthly Donations
- Monthly Construction Report and Change Order Report
- Monthly Ledger is posted
- Monthly posting of Board meetings and Finance Committee Meetings and Minutes
SAS # 99 Auditor to evaluate the entity’s programs and controls that address the identified risks of material misstatement

- The evaluation of the District’s controls that mitigate the identified fraud risks.
- Controls such as:
  - Segregation of duties,
  - Information reported,
  - Preventive controls,
  - Detective Controls
  - Assertive controls
LISD Fraud Program

- Statement of Auditing Standard # 99
- SAS #99 Presentation
- Risk Assessment Procedures
- Template for Internal Controls
- Letters to Vendors (Fraud internal control questionnaire file)
- Employee Conflict of Interest Disclosure Forms
- Other Policies and Checklists useful for administrators in establishing internal controls
- a) LISD Procedures for Initiating a purchase commitment
   b) Procedure for Electronic Authorization Forms
   c) Checklist and Procedures for Grants and Contract and Bank Account
   d) Purchasing Guide Summary of Policies
   e) Standard Conditions for Purchases
   f) Sole Source Affidavit
SAS# 99 Requires to assess the risks of material misstatement due to fraud throughout the audit and to evaluate at the completion of the audit whether the accumulated results of auditing procedures and other observations affect the assessment.

☐ Auditors require the identification of any situations that affect the assessment.

☐ At LISD, there is constant communication and review of controls.
SAS# 99 provides guidance of communicating fraud to the audit committee

☐ All fraud is reported .. No matter how severe or insignificant.

☐ At LISD, we have a policy that requires each person to report it. We further require each staff member to sign at the beginning of the year.
Other related legislation

- **Gramm-Leach-Bliley Act**
  - **Sec. 6801. Protection of nonpublic personal information**
    - (a) Privacy obligation policy
    - It is the policy of the Congress that each financial institution has an affirmative and continuing obligation to respect the privacy of its customers and to protect the security and confidentiality of those customers' nonpublic personal information.

- **Sarbanes-Oxley Act** (SOX)
  The **Sarbanes-Oxley Act of 2002** (Pub. L. No. 107-204, 116 Stat. 745, also known as the **Public Company Accounting Reform and Investor Protection Act of 2002** and commonly called **SOX** or **SarbOx**; July 30, 2002) is a United States federal law passed in response to a number of major corporate and accounting scandals including those affecting Enron, Tyco International, and WorldCom (now MCI).

- **HIPAA**
  Title II of HIPAA, the Administrative Simplification (AS) provisions, requires the establishment of national standards for electronic health care transactions and national identifiers for providers, health insurance plans, and employers.

- **FISMA**
SOX

- Major financial failures
  - Enron
  - WorldCom

- Major legislation: **Sarbanes-Oxley Act of 2002**
  - Public Companies Accounting Oversight Board
    - Impact on the AICPA’s role in audit standard setting
    - Fee-based financial support
  - CEOs and CFOs must certify financial statement disclosures
  - Section 404 requires companies to document adequate internal controls and procedures
Under SOX, Auditors required to:

**Required by the SEC to include**

1. A statement of management’s responsibilities for established and maintaining an adequate system
2. Identification of the framework used to evaluate the internal controls
3. A statement as to whether or not the internal control system is effective as of year-end
4. The disclosure of any material weaknesses in the system
5. A statement that the company’s auditors have issued an audit report on management’s assessment
The Public Company Accounting Oversight Board

☐ Created by the Sarbanes-Oxley Act
☐ An arm of the SEC
☐ 5 members: 2 CPAs, 3 non-CPAs
☒ Promulgates auditing standards for companies subject to the Sarbanes-Oxley Act
  ■ AICPA still issues auditing standards for non-public companies
Going Forward in LISD

- Certifies Financial Statements each month
- Evaluates Internal Controls System and Procedures each year
- Posts Check register on the Web
- Implements Conflict of Interest Program
- Implements Fraud awareness and Prevention Program
Sources

- http://www.laredoisd.org/departments/finance/fogfy0607.htm
- www.aicpa.org

Questions and Summary.