As part of the audit of cash and other liquid assets, you may now complete the following exercises contained in the Biltrite audit practice case:

Module VIII: Dallas Dollar Bank—bank reconciliation

Module IX: Analysis of interbank transfers

Module X: Analysis of marketable securities

Module VIII: Dallas Dollar Bank Reconciliation

Biltrite maintains two general demand deposit accounts and a payroll account. One of the general demand deposit accounts and the payroll account are with Dallas Dollar Bank. The second demand deposit account is with Bank Two, the Chicago bank from which Biltrite obtained the $45 million loan referred to previously. As part of the cash audit, Derick has asked you to reperform the reconciliation of all three of the bank accounts for December 2009, and to do an analysis of inter-bank transfers between Dollar Bank and Bank Two.

Recall that Biltrite has reconciled all bank accounts for each of the 12 months. You will begin, therefore, with the company's documentation of its December 2009 reconciliations.

Requirements

1. Using the spreadsheet program and downloaded data, retrieve the file labeled "Bank." Briefly examine the following documentation in this file:

   - WP 1—Cash on hand and in banks;
   - WP 1.B—Bank reconciliation—Dallas Dollar Bank; and
   - WP 1.C—Inter-bank transfer schedule.

   Scroll to WP 1.B, "Bank Reconciliation—Dallas Dollar Bank." Does the Dollar Bank account reconcile for December? What are the possible causes for nonreconciliation?
2. In tracing cash disbursements from the December check register to the bank statement, you learn that check 44264, in the amount of $642,752, was recorded incorrectly as $651,752. Incorporate this misstatement into the appropriate section of the bank reconciliation. Does the account reconcile after you have made this correction? Assuming check 44264 was in payment of accounts payable (refer to Exhibit BR.16), draft the necessary audit adjustment at the bottom of your document.
3. Print the bank reconciliation document.
4. Scroll to WP 1 and record the audit adjustment in the "audit adjustments" column of the lead schedule.
5. The deposit in transit, as well as all but the last two checks outstanding at December 31, cleared with the bank cutoff statement. What specific audit objectives does obtaining a cutoff statement directly from the bank support? If the cutoff bank statement covered the period 1/1/10 through 1/21/10 and the deposit in transit was credited 1/12/10, would you be concerned? If so, why? What additional procedures would you apply to allay your concerns? Note on document WP 1.B that Dollar Bank credited the deposit in transit on 1/3/10.

Module IX: Analysis of Interbank Transfers

Requirements

1. Using the spreadsheet program and downloaded data, retrieve the file labeled "Bank." Scroll to WP 1.C, "Inter-bank Transfer Schedule." Cheryl Lucas, a member of the Denise Vaughan & Co. audit team, prepared this document. As part of your audit training, Derick asks that you examine and review the document and determine the need for possible audit adjustments and reclassifications.
   a. What is the purpose of analyzing inter-bank transfers for a short period before and after the balance sheet date?
   b. Identify possible audit adjustments and reclassifications by examining WP 1.C. Assume that Bank Two check 127332 was dated December 31, 2009, deposited on that date, and also credited by Dollar Bank on December 31, 2009.
   c. As noted previously, Lawton had borrowed $3 million from Biltrite in April 2008, and had planned to repay the loan before December 31, 2009. Did he really repay the loan in December? Do you think the check drawn on Bank Two was reflected as an outstanding check in the 12/31/09 Bank Two reconciliation? Do you think the check was recorded as a December disbursement? If not, why not? (*Hint:* Remember that the loan agreement with Bank Two requires a $10 million compensating balance at all times.)
2. Draft Audit Reclassification B at the bottom of WP 1.C.
3. Print the inter-bank transfer document.
4. Scroll to WP 1. Record Reclassification B from requirement (2) in the reclassification column of the lead schedule. Does the reclassification place Biltrite in default on the loan agreement? If so, what further audit procedures might you elect to apply at this time?
5. Print the lead schedule.

Module X: Analysis of Marketable Securities

Although the addition of the Waistliner Stationary Bike to the product line helped somewhat in increasing Biltrite's fall and winter revenue, business remains quite seasonal, producing large amounts in idle funds to be invested temporarily after the spring and summer bicycle sales seasons have ended. Marlene McAfee, the Biltrite treasurer, usually invests in marketable securities in mid-August and holds them until mid-January. They are sold in late January and February to finance spring inventories of bicycles. McAfee's goals in acquiring short-term investments are to maximize return while minimizing risk of loss from wide temporary price fluctuations. For this reason, the portfolio is limited to debt securities rated AA and above, and common stocks of "blue-chip" companies.

As of December 31, 2009, the portfolio consisted of the following holdings:

Security	12/31/09 Carrying Value	12/31/09 Market Value
Transco, Inc. Preferred	$ 804,024	$ 810,000
Jolly Roger Amusement Parks Common	720,000	660,000
Pets 'R' Us Common	736,000	742,000
General Department Stores Common	660,000	550,000
AT&T 8% Debenture Bonds	930,000	942,000
Daimler/Chrysler 11% Debenture Bonds	1,150,000	1,131,000
Cleveland Electric 9% Debenture Bonds	2,000,000	2,066,000

Requirements

1. Using the spreadsheet program and downloaded data, retrieve the file labeled "Security." Do you think McAfee's securities portfolio is consistent with her stated goals of "maximizing return while minimizing risk of loss from temporary price fluctuations"? Justify your answer.
2. What determines whether marketable securities are to be classified as current or noncurrent on the balance sheet?
3. What are the objectives in the audit of marketable securities? What are the most relevant assertions for the auditor to examine? Examine the audit legends at the bottom of document 2. Have the objectives been satisfied?
4. Enter the market data for each security held at December 31, 2009.
5. Add an audit legend (and explain it at the bottom of the worksheet) regarding how market was determined.
6. Draft Audit Adjustment 8 at the bottom of WP 2 to recognize the understatement of interest revenue. The discrepancy results from failure to recognize accrued interest at 12/31/09 (debit account 1205, "Accrued Interest Receivable").
7. Draft Audit Adjustment 9 to adjust the loss on decline of market value to reflect the corrected amount. The wide disparity in this instance arises because Biltrite, in adjusting to market at 12/31/09, compared market at 12/31/09 with the cost of the 12/31/08 portfolio, rather than comparing 12/31/09 market with 12/31/09 carrying values. For this adjustment, use account 9702, "Loss on Decline of Market Value of Securities," and account 1102, "Allowance for Decline of Market Value of Securities."
8. Print your document.

13

Audit of Long-Lived Assets and Related Expense Accounts

LEARNING OBJECTIVES

The overriding objective of this textbook is to build a foundation with which to analyze current professional issues and adapt audit approaches to business and economic complexities. Through studying this chapter, you will be able to:

1. Identify the accounts and relevant assertions in the long-lived asset cycle.
2. Describe the approach an auditor would take to perform an integrated audit in the long-lived asset cycle.
3. Identify risks to reliable financial reporting in the long-lived asset cycle and explain how management can manage earnings through fixed-asset accounts.
4. Describe how to use preliminary analytical procedures to identify possible misstatements in the accounts associated with long-lived assets.
5. Describe why it is important for the auditor to develop an understanding of internal controls, identify controls typically present in the long-lived asset cycle, and identify tests of controls used to test the effectiveness of controls over fixed assets.
6. Describe the substantive audit procedures that should be used to test long-lived assets and related accounts.
7. Describe the substantive audit procedures that should be used to test for the impairment of long-lived assets.
8. Discuss the risks associated with intangible assets and natural resources and the approach to auditing intangible assets and natural resources.
9. Discuss the risks associated with lease accounting and the audit approach for leases.
10. Apply the decision analysis and ethical decision-making frameworks to situations involving the audit of long-lived asset accounts.

CHAPTER OVERVIEW

In this chapter, we present a general discussion of risks and audit approaches related to long-lived assets and related expenses, intangibles, natural resources, and leases. In terms of the audit opinion formulation process, this chapter involves Phases III and IV, that is, obtaining evidence about controls and substantive evidence about long-lived asset account assertions. Auditors must consider the possibility that management may manage earnings by manipulating fixed-asset or lease accounts. Although types of fixed assets vary widely, there is a commonality in the audit approach to them. Assets are subject to impairment testing each year.