

## Ignore the Error? Teaching Notes

### *What Are the Relevant Facts?*

1. Kelsey, the audit senior, knows a material cutoff error exists in Compo's financial statements.
2. Compo, a major client of the CPA firm, does not want to make an adjustment for the cutoff error.
3. Contrary to the firm's policy, Bruce, the audit manager, has asked Kelsey not to document the cutoff error.

### *What Are the Ethical Issues?*

1. Kelsey has a professional responsibility to document proposed material audit adjustments. Kelsey has been asked by the supervisor to ignore this requirement. Should Kelsey violate professional and personal standards of integrity to comply with the request?
2. What responsibility does Kelsey have to inform affected parties of the request to violate firm policy?

### *Who Are the Primary Stakeholders?*

- Kelsey, the audit senior
- Bruce, the audit manager
- The partner in charge of the audit and the entire CPA firm
- The owners of Compo Corporation (family members or others holding shares in the company)
- Third-party users of Compo's financial statements
- Compo Corporation employees

### *What Are the Possible Alternatives?*

Kelsey can:

1. Not document the cutoff error as requested.
2. Document the error but rationalize that it is not material.
3. Document the cutoff error in compliance with firm policy.

4. Discuss the relevant facts directly with the partner in charge of the audit.

### *What Are the Ethics of the Alternatives?*

- Based on a utilitarian costs and benefits analysis, for each alternative:
  1. What are the benefits and costs to each stakeholder?
  2. Do the net benefits exceed the net costs to all stakeholders?
- Based on a "rights" perspective, for each alternative:
  1. What are the rights of each stakeholder?
  2. What are the responsibilities of Kelsey, Bruce, the CPA firm, and Compo?
  3. Which alternative would you prefer if you were relying on Compo's financial statements for decision making?
- Considering a "justice" point of view, for each alternative:
  1. For each stakeholder, what are the burdens and benefits
  2. Which alternative most fairly distributes the burdens and benefits among the stakeholders?

### *What Are the Practical Constraints?*

1. Kelsey's supervisor wants the material cutoff issue to be ignored.
2. Compo, the largest client, wants this issue to be ignored, so the CPA firm may lose this client.
3. On the other hand, such actions violate firm policy. What if the partners find out that policy has been violated?

### *What Actions Should Be Taken?*

1. What action would you take if you were Kelsey? Why?