**Chapter 2**

**The CPA Profession**

In Chapter 1, students learned about the demand for assurance services and the different types of audits. Chapter 2 describes the CPA profession, and the standards that govern audit performance.

**Chapter Opening Vignette — “Good Auditing Includes Good Client Service”**

This vignette demonstrates that auditors are expected to provide value-added services to clients. The vignette also challenges preconceived notions about the role of auditors, and illustrates that students will be in a position to assist clients immediately upon entering the profession. We use this as an opportunity to discuss the performance expected of new auditors, and that students need to be familiar with real-world activities by reading such sources as the *Journal of Accountancy* and *The Wall Street Journal*.

**Certified Public Accounting Firms and their Activities** (page 26, page 27)

Many students will be familiar with the “Big 4” and the activities of these firms, but many will not. Most students will have little knowledge of other CPA firms. In a brief class discussion, we highlight for students:

 The four categories of CPA firms

 The names of the Big 4, plus several major firms in the other categories that recruit at our universities

 Changes occurring in each category of firms

We then ask students for their perceptions about whythere have been changes among the Big 4 and National firms. We use this as an opportunity to discuss the forces affecting the profession. We are careful not to offer opinions about the desirability of these changes, or preferences for one firm or category of firm versus another.

We briefly mention the major activities of the firms (audit and assurance services, taxes, and consulting). We also note that consulting and other services are once again growing in importance at the Big 4, although they are restricted from providing many services to public company audit clients. **Table 2-1** (page 26) is helpful in describing the relative size of firms in each category, and the relative importance of each activity. We encourage students to learn more about the major CPA firms by visiting their web sites.

**(See Table 2-1; shown on Slide 2-8)**

**Structure of CPA Firms** (page 28)

We briefly describe the six organizational structures of CPA firms. We emphasize the use of limited liability corporations and partnerships. We ask students to evaluate the desirability of these organizational forms as a potential new entrant into the profession, from the perspective of a partner, and the perspective of an investor.

We use **Table 2-2** (page 29) to describe the typical positions in a CPA firm, the responsibilities of the position, and how long a person stays in each category. We emphasize that technology has increased the responsibility given new staff, and that advancement is fairly rapid. **Slide 2-12** provides an overview of the hierarchy of a typical CPA firm.

**(See Table 2-2)**

**(See Slide 2-12)**

**Sarbanes–Oxley Act and PCAOB** (page 30)

We discuss the origins of the Sarbanes–Oxley Act and the significant changes it has brought to financial reporting and the accounting profession. We then discuss the role of the PCAOB in establishing auditing and quality control standards for registered firms with public company audit clients. We clarify that the PCAOB oversight is limited to public company audits. We also note that the PCOAB adopted GAAS as interim auditing standards, and that the PCAOB is establishing new auditing standards for public company audits.

**Securities and Exchange Commission (SEC)** (page 30)

The four most important things to explain to students about the SEC are:

1. Role of the SEC in general and as it relates to auditors.

2. What companies are required to report to the SEC.

3. Differences between the AICPA and SEC and relation between the PCAOB and SEC.

4. How the SEC influences auditing.

**AICPA** (page 31)

We talk briefly of the role of the AICPA, with emphasis on its responsibility for the CPA exam and establishing standards and rules. We encourage students to consider joining the AICPA as a student affiliate member, which is explained more fully on the AICPA website.

**International and U.S. Auditing Standards** (page 32)

We discuss the role of auditing standards and introduce the International Auditing and Assurance Standards Board. We note that globalization has increased the need for uniform international accounting and auditing standards. We discuss how the AICPA Auditing Standards Board (ASB) has revised most of its standards to converge with the international standards and how the PCAOB considers existing international standards as it develops PCAOB standards. The vignette at the top of page 33 provides an overview of the approach the ASB is using to converge their standards with international standards.

We use **Figure 2-1** (page 34) to indicate when international, AICPA (U.S. GAAS), and PCAOB standards apply. Homework problems 2-20 and 2-22 are also useful to cover this concept. We emphasize the similarity of the standards.

**(See Figure 2-1; shown on Slide 2-26)**

**Generally Accepted Auditing Standards** (page 34)

First, it is useful to introduce the new Principles that provide the framework for generally accepted auditing standards. We review each of these Principles as described on pages 34 through 38 and help students see how each of the Principles in the AICPA auditing standards reconcile to the ten GAAS standards still used in PCAOB standards. **Figure 2-2** (page 36) provides a great summary of that reconciliation. Alternatively, the summary on **OH-2-1** may be helpful as well.

**(See Figure 2-2)**

**(See OH-2-1)**

Review Questions 2-8 and 2-9 can be helpful for class discussion. Students are told they are required to know the core elements of the Principles and ten GAAS standards, but that they do not need to memorize them word for word. Problem 2-21 is a good one to help students understand the application of the Principles that provide the framework for GAAS to practice.

**Statements on Auditing Standards** (page 38)

We briefly explain the role of Statements on Auditing Standards. We explain the classification systems used to allow students to refer to SASs when necessary. We also note that the ASB Clarity Project has resulted in a new AU-C numbering system for the Codification of Statements on Auditing Standards that aligns the organizational structure of AICPA auditing standards with the structure used for international standards.

**Quality Control** (page 39)

With the increased emphasis on quality control in the profession, we discuss both quality control and peer review briefly. Emphasize the purposes, benefits, and costs of both. Problem 2‑19 is useful for defining the elements of quality control.

Students often have difficulty understanding the relation between quality control and peer review. A useful analogy is to describe peer review as an audit of the firm’s quality control system. **Figure 2-3** (page 41) is helpful in describing the relation between audit standards, quality control, peer review, and the AICPA practice and quality centers. We clarify that PCAOB inspections relate to public company audits, and peer review relates to other areas of a firm’s assurance practice.

**(See Figure 2-3; shown on Slide 2-36)**

**Summary**

After covering Chapters 1 and 2, students have an understanding of the value of audit and assurance services, and some of the factors that affect auditor performance. **Figure 2-4** (page 42) provides a useful summary of these factors, and can be used to introduce the concepts of professional ethics and legal liability covered in Chapters 4 and 5.

**(See Figure 2-4; shown on Slide 2-37)**

**CHAPTER 2**

2-5

**CROSS-REFERENCE OF LEARNING OBJECTIVES AND PROBLEM MATERIAL**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **LEARNING OBJECTIVES** | **REVIEW QUESTIONS** | **MULTIPLE CHOICE QUESTIONS** | **DISCUSSION QUESTIONS AND PROBLEMS** | **CASES** |
| **2-1** Describe the nature of CPA firms, what they do,  and their structure. | 2-1, 2-2 | 2-15 |  |  |
| **2-2** Understand the role of the Public Company Accounting Oversight Board and the effects of the Sarbanes–Oxley Act on the CPA profession. | 2-3, 2-7 | 2-15 |  |  |
| **2-3** Summarize the role of the Securities and Exchange Commission in accounting and auditing. | 2-4 | 2-15 |  |  |
| **2-4** Describe the key functions performed by the AICPA. | 2-5, 2-6, 2-7 |  |  |  |
| **2-5** Understand the role of international auditing  standards and their relation to U.S. auditing standards. | 2-7, 2-11 |  | 2-20, 2-22 |  |
| **2-6** Use U.S. auditing standards as a basis for further study. | 2-8, 2-9, 2-10 | 2-16 | 2-18, 2-20, 2-21 |  |
| **2-7** Identify quality control standards and practices  within the accounting profession. | 2-2, 2-12,  2-13, 2-14 | 2-17 | 2-19 |  |

**RELATIONSHIP OF PRINCIPLES AND**

**PCAOB’S 10 GAAS**

**PRINCIPLES IN AICPA PCAOB 10**

**AUDITING STANDARDS GAAS STANDARDS**

 **PURPOSE OF AUDIT NOT EXPLICIT IN 10 GAAS**

**(DESCRIBE PURPOSE IS TO OFFER OPINION ON F/S)**

 **RESPONSIBILITIES 3 GENERAL STANDARDS**

**(DESCRIBE CHARACTERISTICS OF AUDITOR)**

 **PERFORMANCE 3 FIELDWORK STANDARDS**

**(DESCRIBE WORK TO BE DONE IN AUDIT)**

 **REPORTING 4 REPORTING STANDARDS**

**(DESCRIBE NATURE OF WHAT AUDITOR REPORTS)**