

Case 18-10 — Handout 1

Antelope Run Inc. — Controls With a Review Element

Note that this handout is based on a form that audit teams can use to document their tests and evaluation of the design and operating effectiveness of controls in accordance with PCAOB standards. Although the form is presented in its entirety for informational purposes, certain input boxes of the form have been shaded gray because they are either given as case facts or are otherwise not applicable to this activity in the case.

Component A — Control Description

Control Activity — Summary Description

C-5: Antelope Run Inc.'s (Antelope's) fitness trackers business planning committee (the "BPC") meets to review, challenge, and approve the revenue forecast for the fitness trackers reporting unit (Fit Stride) for appropriateness using historical performance and its knowledge of the company's strategic plans as well as industry projections and peer-company data.

Control Description — Detailed Description of How the Control Is Expected to Be Performed

To review, challenge, and approve the revenue forecast for each fitness tracker product and for Fit Stride overall, the BPC performs the following procedures:

Step 1 — Sales Volume

Step 1a: For sales volume, the BPC will compare the historical sales volumes for each product to the forecasted sales volume by comparing (using judgment) the year-to-year percentage change in volume to identify any anomalies. The BPC will pose questions to the Fit Stride director of sales and marketing (the "Director") for further explanation to understand what is driving the forecasted sales volume.

Step 1b: For sales price, the BPC will compare the historical sales price to the forecasted sales price by comparing the year-to-year percentage change in price to identify anomalies. The BPC will pose questions to the Director for further explanation to understand what is driving the forecasted sales price changes.

Step 1c: The BPC will compare the forecasted price of each product to competitor prices and, using judgment, identify differences to investigate. To complete this review, the BPC uses the following report:

Forecasted sales price per unit versus competitor sales prices per unit for each fitness tracker product.

Step 1d: The BPC will also perform a retrospective review by comparing the forecasted revenues by product for each of the past three years to actual sales revenue in those years to evaluate (using judgment) the reasonableness of the forecast.

Step 2 — Revenue

The BPC reviews the revenue forecast for Fit Stride.

Step 2a: The BPC will (1) compare the historical revenues to the forecasted revenues for Fit Stride overall and (2) compare the most recent three years' revenues to the annual percentage change in forecasted revenues to identify anomalies. The BPC will pose questions to the Director for the respective reporting units for further explanation to understand what is driving the forecasted revenue.

Step 2b: The BPC will also compare the forecasted revenues to the prior-year forecast for Fit Stride overall to identify any anomalies.

Step 2c: The BPC will also compare the percentage change in forecasted revenues to industry forecasts (e.g., *Heart Healthy Quarterly* publication and peer-company forecasts published by industry analysts) to identify any anomalies.

Step 2d: Lastly, the BPC will also perform a retrospective review by comparing the forecasted revenues for Fit Stride for each of the past three years to actual sales revenue in those years to evaluate the reasonableness of the revenue forecast.

Step 3 — Revise Revenue Forecast for Fit Stride

Risk of Material Misstatement Addressed by the Control	Risk of Material Misstatement Classification	Significant
<p>Management’s revenue projections and revenue growth rate assumptions that are used in various estimates may not be based on the best and most supportable information and contain a high degree of estimation uncertainty. Specifically, management’s estimates of revenue growth are not only aggressive when compared to the historical performance of the Fit Stride products, but they also incorporate subjective assumptions associated with revenue growth of the new Fit Belt product line.</p>		
Significant Account(s) and Related Assertion(s) Addressed		
<p>Significant Account: Goodwill Related Assertion: Valuation and Allocation</p>		

Component B — Test of Design

Procedures Performed to Test the Design of the Control						
Test of design for each step of the review:						
Step 1:	Inquiry	X	Observation	X	Inspection	X
<p>To evaluate the design effectiveness of this control, we attended the annual BPC review meeting that took place on September 15 of the current year. The meeting included an evaluation of the revenue forecast assumptions used in management’s projections on a product-by-product basis. We attended the meeting to observe the nature of the review performed by the BPC of the revenue forecast for Fit Stride by product. We also inspected the revenue forecast detail schedules (see working paper XXXX for each schedule used). We noted that each schedule included fluctuation analyses for each of the fitness tracker products, and that detail was at an appropriate level to facilitate the discussions that took place at the meeting. All variances outside management’s established thresholds were discussed by the BPC.</p>						

Step 2:	Inquiry	X	Observation	X	Inspection	X
<p>To evaluate the design effectiveness of this control, we attended the annual BPC review meeting that took place on September 15 of the current year. The meeting included an evaluation of the revenue forecast assumptions used in management's projections for Fit Stride on an overall basis. We attended the meeting to observe the nature of the review performed by the BPC over Fit Stride revenue forecast. We also inspected the revenue forecast detail schedules (see working paper XXXX for each schedule used). We noted that each schedule included fluctuation analyses for each of the fitness tracker products, and that detail was at an appropriate level to facilitate the discussions that took place at the meeting. All variances outside management's established thresholds were discussed by the BPC.</p>						
Step 3:	Inquiry	X	Observation	X	Inspection	X
<p>During the annual review meeting, in addition to observing the BPC's decision and agreement to reduce the fitness tracker reporting unit revenue forecast, we also inspected the meeting minutes and subsequent e-mail communications among the members of the BPC (dated October 10) to obtain evidence that the appropriate actions were taken after the meeting to adjust the forecast. We inquired with Antelope's controller and director of financial planning and analysis (FP&A), who corroborated that the forecast was adjusted for the recommendations that were made at the meeting.</p>						

Component C — Evaluation of Design

How the Control Satisfies the Control Objectives

Document whether the control satisfies the corresponding control objective, including whether it addresses the risks of material misstatement to the relevant assertion of the significant account or disclosure.

Risk Addressed by the Control

On the basis of our understanding of the detailed description of this control above, we have determined that the entity has a sufficiently precise control process to ensure that the revenue forecast for Fit Stride is reviewed, challenged, and approved. As such, the purpose of the control is appropriate given the risks associated with it.

Competence and Authority of the Person(s) Performing the Control

Document the person(s) who performs the control, including the competence and authority of the person(s).

This content is not included for purposes of the case study; please do not consider.

Frequency and Consistency of the Performance of the Control

Document the frequency and consistency of performance of the control, that is, whether the review occurs often enough to prevent or detect misstatements before they have a material effect on the financial statements.

This content is not included for purposes of the case study; please do not consider.

Level of Aggregation and Predictability

Document the appropriateness of the level of aggregation and predictability of the control.

This content is not included for purposes of the case study; please do not consider.

Criteria for Investigation (i.e., threshold) and Process for Follow-Up

Document the factors affecting the precision of the review, including the objective of the review and the appropriateness of the expectations, level of aggregation, and criteria for investigation for identifying potentially material misstatements. Also document the steps involved in identifying, investigating, and resolving significant differences from expectations.

As noted in the detailed steps of the control, the BPC investigates the reasonableness of forecasted results as compared to historical, peer, and industry performance, with consideration of entity-specific events. If any variances are noted between the forecasted results and these other data points, the BPC will discuss and evaluate whether an adjustment to the forecast is necessary. If an adjustment is deemed necessary, the forecast will be adjusted in the Hyperion Financial Management software (Hyperion).

Dependency on Other Control(s) or Information

Is the control dependent on other controls?

If yes, indicate which other control(s), where the other control(s) is (are) tested, and the conclusion reached on the design and operating effectiveness of the control(s).

This content is not included for purposes of the case study; please do not consider.

Information Used in the Review

Is the effectiveness of the control dependent on information used in the review?

If yes, identify the controls that address the accuracy and completeness of the information used in the review, where this information is tested, and the conclusions reached as a result of that testing.

This content is not included for purposes of the case study; please do not consider.

Design Effectiveness Conclusion

Effective

If design effectiveness conclusion is deemed ineffective, document the basis for this conclusion.

N/A

Risk Associated With the Control

Higher

Considering the factors in paragraph .47 of PCAOB Auditing Standard (AS) No. 2201, *An Audit of Internal Control Over Financial Reporting That Is Integrated With an Audit of Financial Statements*, conclude on the risk associated with the control.

Document the basis for the conclusion on the risk associated with the control.

As noted above, this control is designed to address a significant risk of material misstatement. We considered the risk associated with the control to be “higher” on the basis of (1) the nature of misstatements that the control is intended to prevent (valuation errors), (2) the complexity of the revenue forecasting process for Antelope’s Fit Stride, (3) the specialized expertise required to operate the control effectively, and (4) the significance of the judgments that are made in connection with its operation.								
Component D — Test of Operating Effectiveness								
Planned Nature, Timing, and Extent of Operating Effectiveness Testing								
Nature of Procedures								
For each step, we will supplement the procedures performed as a part of the design effectiveness testing to obtain evidence of operating effectiveness through the following additional procedures:								
Step 1:	Inquiry	X	Observation	X	Inspection	X	Reperformance	X
We will attend the BPC meeting to observe the performance of this control. In addition, we will inspect the information reviewed and discussed as part of that meeting and reperform the review of the variances in the revenue forecast by product as discussed by the BPC.								
Step 2:	Inquiry	X	Observation	X	Inspection	X	Reperformance	X
We will attend the BPC meeting to observe the performance of this control. In addition, we will inspect the information reviewed and discussed as part of that meeting and reperform the review of the variances in the revenue forecast for Fit Stride as discussed by the BPC.								
Step 3:	Inquiry	X	Observation	X	Inspection	X	Reperformance	X
We will inspect the meeting minutes and any supporting documentation, if applicable, and verify that feedback provided by the BPC was incorporated into the final revenue forecast by product and by reporting unit. Any revisions noted will be traced from the draft revenue forecast to the final revenue forecast to determine whether they were appropriately addressed. To understand how the revisions were to be made, we will inspect the instructions noted by the BPC members in subsequent e-mail communications. We will also perform inquiries with BPC members to corroborate that the adjustments to the forecast were consistent with what they recommended at the meeting.								
Timing and Extent of Procedures		Because this control operates annually, we will test that instance of the control.						

Control Activity Testing

For each step, we will supplement the procedures performed as a part of the design effectiveness testing to obtain evidence of operating effectiveness through the following additional procedures:

Selection Number	Selection Date	Procedures Performed	Exception or Deviation?
1	N/A	Step 1: We reperformed the review of the analysis by comparing the forecasted revenue amounts to historical	No
		<p>amounts for the Fit Band product as well as reperforming the retrospective review of the prior forecasted revenues versus actual sales revenues for the prior three years for the Fit Band. Our conclusions were consistent with those reached by management at the meeting. When applicable, we inspected the board of directors' second quarter meeting minutes to corroborate the items discussed by management during the meeting with respect to the Fit Band product.</p> <p>Step 2: We reperformed the review of the analysis by comparing the forecasted revenue amounts to historical amounts for Fit Stride overall as well as reperforming a retrospective review of the prior forecasted revenues versus actual sales revenues for the prior three years for Fit Stride overall. We recalculated the differences on the reports, noting that the variances were consistent with those discussed at the meeting.</p> <p>Step 3: No additional operating effectiveness procedures were deemed necessary beyond those procedures performed in the test of design.</p>	
Operating Effectiveness Testing Conclusion			
Conclusion. If deemed ineffective, document the basis for this conclusion.	Effective. N/A		