

- d. Negative confirmations do not produce evidential matter that is statistically quantifiable.
- e. All of the above
- 10-53 A customer confirmed its balance by fax. Which of the following would not reduce the risk associated with the response? — LO 10
- Consider the fax response to be an exception.
 - Examine subsequent collections of the account.
 - Request the customer to mail the original confirmation to the auditor.
 - Consider the fax to be an acceptable confirmation response.

Discussion and Research Problems

- 10-54 (Revenue Recognition) Judgments about whether revenue should be recognized are among the most contentious that an auditor faces. Following are a number of situations in which the auditor will be required to either acquire additional information or make decisions about the amount of revenue to be recognized. — LO 2

Required

- Identify the primary criteria the auditor should use in determining revenue to be recognized.
- For each of the scenarios:
 - Identify the key issues to address in determining whether revenue should be recognized.
 - Identify additional information the auditor may want to gather in making a decision on revenue recognition.
 - Based only on the information presented, develop a rationale for either the recognition or nonrecognition of revenue.

Revenue Recognition Scenarios

- AOL sells software that is unique as an Internet provider. The software contract includes a service fee of \$19.95 for up to 500 hours of Internet service each month. The minimum requirement is a one-year contract. The company proposes to immediately recognize 30 percent of the first-year's contract as revenue from the sale of software and 70 percent as Internet services on a monthly basis as fees are collected from the customer.
- Modis Manufacturing builds specialty packaging machinery for other manufacturers. All of the products are high-end and range in sales price from \$5 million to \$25 million. A major customer is rebuilding one of its factories and has ordered three machines with total revenue of \$45 million. The contracted date to complete the production was November and the company met the contract date. The customer acknowledges the contract and confirms the amount. However, because the factory is not yet complete, they have requested that Modis hold the products in their warehouse as a courtesy to the company until their building is complete.
- Standish Stoneware has developed a new low-end line of bakeware products that will be sold directly to consumers and to low-end discount stores (but not Wal-Mart). The company had previously sold high-end silverware products to specialty stores and has a track record for returned items from the high-end stores. The new products tend to have more defects, but the defects are not necessarily recognizable in production. For example, the products are more likely to crack when first used in baking. The company does not have a history of returns from these products but because the products are new, the company grants each customer the right to return the merchandise for a full refund or replacement within one year of purchase.
- Omer Technologies is a high-growth company that sells electronic products to the custom copying business. It is an industry with high innovation, but Omer's