**Capstone Research Project**

**Scenario**

You are the partner in an accounting firm hired to audit a Fortune 1000 company. The initial public offering (IPO) of the company was approximately five years ago and the company is concerned that, in fewer than five years after the IPO, a restatement may be necessary. During your initial evaluation of the client, you discover the following:

* The client is undergoing a three-year income tax examination by the Internal Revenue Service. A significant issue in the IRS audit involves inventory write-downs on the tax returns that are not included in the financial statements. Because of the omission of the transaction, the IRS is labeling the treatment of the write-down as fraud.
* The company has a share-based compensation plan for top-level executives consisting of stock options. The value of the options exercised during the year was not expensed or disclosed in the financial statements.
* The company has several operating and capital leases in place, and the CFO is considering leasing a substantial portion of the assets for future use. The current leases are arranged using special purpose entities (SPEs) and operating leases.
* The company seeks to acquire a global partner, which will require IFRS reporting.
* The company received a request from Securities and Exchange Commission (SEC) for additional supplemental information regarding the financial statements submitted with the IPO.

**Instructions**

Write an 8–10 page paper in which you:

* Evaluate any damaging financial and ethical repercussions of failure to include the inventory write-downs in the financial statements. Prepare a recommendation to the CFO, evaluating the impact of a civil fraud penalty on the corporation as a result of the IRS audit. Include essential internal control procedures to prevent fraudulent financial reporting from occurring, as well as the major obligation of the CEO and CFO to ensure compliance.
* Examine the adverse effects on stakeholders and the financial statements of an IRS audit resulting in additional tax and penalties or subsequent audits. Assume that the subsequent audit and/or additional tax and penalties stem from the taxpayer’s use of an inventory reserve account, applying a 10 percent reduction to inventory over three years.
* Discuss the applicable federal tax laws, regulations, rulings, and court cases related to the inventory write-downs and explain the specific relevance of each to the write-down.
* Research the current generally accepted accounting principles (GAAP) regarding stock option accounting. Evaluate the current treatment of the company’s share-based compensation plan based on GAAP reporting. Contrast the financial benefits and risks of the share-based compensation stock option plan to the financial benefits and risks of a share-based stock-appreciation rights plan (SARS). Recommend to the CFO which plan the company should use and provide the correct accounting treatment for each.
* Research the reporting requirements for lease reporting under GAAP and International Financial Reporting Standards (IFRS). Based on your research, create a proposal for future lease transactions to the CFO. Within the proposal, discuss the use of off-the-balance-sheet financing arrangements, capital leases, and operating leases, and indicate the related business and financial risks of each.
* Create an argument for or against a single set of international accounting standards related to lease accounting based on the global market and cross-border leases of assets. Examine the benefits and risks of your chosen position.
* Examine the major implications of SAS 99 based on the factors discovered during your initial evaluation of the company. Provide support for your rationale.
* Analyze the potential for a material misstatement in the financial statements based on the issues identified in your initial evaluation. Make a recommendation to the CFO for the issuance of restated financial statements. Identify at least three significant issues that can result from the failure to issue restated financial statements.
* Examine the economic effect of restatement of the financial statements on investors, employees, customers, and creditors.
* Use at least five quality academic resources in this assignment from the Internet and/or [Basic Search: Strayer University Online Library](https://research.strayer.edu/). Note: Wikipedia and similar websites do not qualify as academic resources.