PCAOB
PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

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Order Instituting Disciplinary Proceedings, Making Findings, and Imposing Sanctions

In the Matter of Sarah C. Martin, CPA,

Respondent.

PCAOB Release No. 105-2021-009

September 17, 2021

By this Order, the Public Company Accounting Oversight Board ("Board" or "PCAOB") is barring Sarah C. Martin, CPA ("Martin" or "Respondent") from being an associated person of a registered public accounting firm[1] and imposing a civil money penalty in the amount of $10,000 on Martin. The Board is imposing these sanctions on the basis of its findings that Martin violated PCAOB rules and standards in connection with the 2017 integrated audit of an issuer's financial statements and internal control over financial reporting ("ICFR") and her subsequent failure to cooperate with the Board's inspection of that audit.

I.

The Board deems it necessary and appropriate, for the protection of investors and to further the public interest in the preparation of informative, accurate, and independent audit reports, that disciplinary proceedings be, and hereby are, instituted against Respondent pursuant to Section 105(c) of the Sarbanes-Oxley Act of 2002, as amended ("Act"), and PCAOB Rule 5200(a)(1).

II.

In anticipation of the institution of these proceedings, and pursuant to PCAOB Rule 5205, Respondent has submitted an Offer of Settlement ("Offer") that the Board has determined to accept. Solely for purposes of these proceedings and any other proceedings brought by or on behalf of the Board, or to which the Board is a party, and without admitting or denying the findings herein, except as to the Board's jurisdiction over Respondent and the

[1] Martin may file a petition for Board consent to associate with a registered public accounting firm after one year from the date of this Order.

subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Disciplinary Proceedings, Making Findings, and Imposing Sanctions ("Order") as set forth below.[2]

III.

On the basis of Respondent's Offer, the Board finds that:[3]

A. Respondent

1. **Sarah C. Martin** was, at all relevant times, a certified public accountant licensed by the Virginia Board of Accountancy (license no. 26944). Martin's CPA license is currently on inactive status. Martin was, at all relevant times, a partner in PricewaterhouseCoopers LLP's ("PwC") Richmond, Virginia office and an associated person of a registered public accounting firm as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(i). She served as the engagement partner for PwC's integrated audit of the Issuer's 2017 financial statements and ICFR.

B. The Issuer

2. The **Issuer** was, at all relevant times, a Virginia corporation and an issuer as that term is defined by Section 2(a)(7) of the Act and PCAOB Rule 1001(i)(iii).

C. Summary

3. This matter concerns Martin's violations of PCAOB rules and standards in connection with the integrated audit of the Issuer's financial statements and ICFR as of and for the year ended December 31, 2017, and during the PCAOB's subsequent inspection of that audit.

4. During the 2017 audit, Martin failed to perform sufficient audit procedures to test the design and operating effectiveness of certain of the Issuer's controls. As a result,

[2] The findings herein are made pursuant to Respondent's Offer and are not binding on any other person or entity in this or any other proceeding.

[3] The Board finds that Respondent's conduct described in this Order meets the conditions set out in Section 105(c)(5) of the Act, 15 U.S.C. § 7215(c)(5), which provides that certain sanctions may be imposed in the event of: (1) intentional or knowing conduct, including reckless conduct, that results in a violation of the applicable statutory, regulatory, or professional standard; or (2) repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standard.

Martin failed to identify numerous control deficiencies that PwC later determined, following a PCAOB inspection, to be material weaknesses in ICFR.

5. Specifically, Martin's failure to perform sufficient audit procedures caused her not to identify 15 material weaknesses. Following PwC's post-inspection ICFR supplemental procedures, the Issuer and PwC combined these 15 individual material weaknesses into two aggregated material weaknesses that existed as of December 31, 2017: one with respect to the accuracy and occurrence of revenue, and a second with respect to the review of cash flow forecasts. The Issuer filed a Form 8-K disclosing that PwC's unqualified 2017 ICFR opinion should no longer be relied upon.

6. In addition, during the PCAOB's inspection of the 2017 Issuer audit, Martin participated in meetings during which PwC personnel provided the PCAOB inspectors with a sensitivity analysis performed during the inspection that PwC personnel claimed had informed the engagement team's work during the audit. Martin knew or should have known that the sensitivity analysis had been created during the inspection and had not informed the team's work during the audit. However, Martin failed to disclose this information to the PCAOB inspectors, in violation of PCAOB rules.

D. Martin Violated PCAOB Rules and Standards During the 2017 Audit of the Issuer's ICFR

7. Martin served as the engagement partner for PwC's 2017 audit of the Issuer. On February 21, 2018, PwC issued unqualified audit opinions on the Issuer's financial statements and ICFR as of and for the year ended December 31, 2017. The Issuer filed PwC's audit report with the Securities and Exchange Commission ("Commission") as part of its 2017 Form 10-K.

8. During the 2017 audit of the Issuer's ICFR, Martin reviewed audit documentation identifying the likely sources of potential misstatement ("LSPMs") for each relevant area of the audit, as well as all of the related walkthrough work papers where the controls that were intended to address those LSPMs were identified and described. Martin also reviewed many, but not all, of the relevant detailed control testing work papers.

9. Based on her review, Martin knew or should have known that the Issuer's controls failed to address the LSPMs she had identified with respect to the accuracy and occurrence of revenue in two of the Issuer's divisions ("Division 1" and "Division 2," respectively) and the review of cash flow forecasts.

10. The PCAOB inspection of the 2017 Issuer audit resulted in the issuance of four comment forms criticizing PwC's ICFR testing. As part of its remediation of the inspection

comments, PwC performed supplemental procedures and identified nine material weaknesses in controls related to the Division 1 revenue cycle and five material weaknesses in controls related to the Division 2 revenue cycle. The Issuer and PwC aggregated these individual material weaknesses into a single aggregated material weakness in controls over the accuracy and occurrence of revenue.

11. During its post-inspection ICFR supplemental procedures, PwC also identified two deficiencies in controls related to cash flow forecasts used in valuing certain of the Issuer's assets. The Issuer and PwC aggregated these deficiencies into a single material weakness in controls over the review of cash flow forecasts.

12. On November 1, 2018, the Issuer filed a Form 8-K stating that it and PwC had re-evaluated the company's ICFR as of December 31, 2017, and identified material weaknesses in the two areas discussed above, and that PwC's 2017 ICFR opinion should no longer be relied upon.

i. Relevant PCAOB Rules and Standards

13. In connection with the preparation or issuance of an audit report, PCAOB rules require that a registered public accounting firm and its associated persons comply with the Board's auditing and related professional practice standards.[4]

14. Section 404 of the Act requires company management to assess and report on the effectiveness of ICFR. The Act also, in certain circumstances, requires a company's independent auditor to attest and report on management's assessment of the effectiveness of ICFR. Effective ICFR provides reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes.[5] However, a company's ICFR cannot be considered effective if one or more material weaknesses in internal control exist.[6]

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[4] PCAOB Rule 3100, *Compliance with Auditing and Related Professional Practice Standards*; *see also* PCAOB Rule 3200, *Auditing Standards*.

[5] AS 2201.02, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

[6] *Id*.

15. PCAOB standards provide that an auditor performing an ICFR audit should test those controls that are important to the auditor's conclusion about whether the company's controls sufficiently address the assessed risk of misstatement for each relevant assertion.[7]

16. "The auditor should test the design effectiveness of controls by determining whether the company's controls, if they are operated as prescribed by persons possessing the necessary authority and competence to perform the control effectively, satisfy the company's control objectives and can effectively prevent or detect errors or fraud that could result in material misstatements in the financial statements."[8] The auditor also should test the operating effectiveness of controls "by determining whether the control is operating as designed and whether the person performing the control possesses the necessary authority and competence to perform the control effectively."[9]

17. When determining whether a control deficiency rises to the level of a material weakness, the auditor should evaluate the effect of compensating controls.[10] "To have a mitigating effect, the compensating control should operate at a level of precision that would prevent or detect a misstatement that could be material."[11]

ii. Controls Over Division 1 and Division 2 Revenue

18. Division 1 and Division 2 contributed 31% and 24%, respectively, of the Issuer's 2017 revenue.

19. During the 2017 audit, Martin and the engagement team identified LSPMs for Division 1 revenue, which included: (1) inaccurate or incomplete entry of sales orders; (2) recognition of revenue for goods or services that were not ordered by customers; and (3) a failure to recognize revenue at the appropriate price.

20. Martin failed to ensure that the engagement team adequately tested whether the Issuer's controls were, in fact, appropriately designed to address these LSPM risks.[12] For example, Martin failed to ensure that the engagement team identified or tested any controls

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7 AS 2201.39.

8 AS 2201.42.

9 AS 2201.44.

10 AS 2201.68.

11 *Id*.

12 *See* AS 2201.42.

over whether the sales order quantities manually recorded in the company's software system were consistent with customer purchase orders.

21. Similarly, while Martin and the engagement team identified two controls that were intended to address the accuracy of prices used to record revenue, neither of these controls tested sales orders in a price range from which the Issuer derived 98% of its Division 1 revenue.

22. For Division 2 revenue, the LSPMs that Martin and the engagement team identified included: (1) inaccurate or incomplete entry of sales orders; (2) recognition of revenue for goods or services that were not ordered by customers; (3) a failure to properly segregate duties; (4) inaccurate recording of cash receipts; and (5) a failure to record cash receipts in the correct period.

23. Once again, while Martin and the engagement team identified several controls that purported to address these LSPM risks, they failed to adequately test whether the Issuer's controls were, in fact, appropriately designed to do so.[13] For example, Martin and the engagement team identified a design deficiency relating to the accuracy of sales order entries and the potential recognition of revenue for goods and services not ordered by customers. In response, Martin and the engagement team identified certain compensating controls upon which they relied to conclude that the deficiency was not a material weakness. However, these compensating controls did not adequately mitigate the risk from the identified control deficiency.[14]

24. One of the controls that PwC identified as compensating was the automatic generation of sequential sales order numbers by the Issuer's software system when a purchase order was manually entered. Martin and the engagement team noted that the control prevented duplicate sales orders, but they did not evaluate the control's failure to address whether the manually-entered order quantities were accurate. The remaining compensating controls identified by Martin and the engagement team likewise failed to adequately address this risk.

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[13] *See id*.

[14] *See* AS 2201.68.

25. Accordingly, Martin failed to ensure that the engagement team adequately tested whether the Issuer's controls were designed in a manner that appropriately addressed the LSPMs identified with respect to Division 1 and Division 2 revenue.[15]

iii. Controls Over Cash Flow Forecasts

26. The Issuer reported a significant investment in a private company representing 7% of the Issuer's total assets as of December 31, 2017 ("Investment"). The Issuer accounted for the Investment using the fair value method, which relied on cash flow forecasts, and recorded a net gain on the Investment of 63% of the Issuer's net income during 2017.

27. In addition, the Issuer recorded a significant acquisition ("Acquisition") during 2017 for which it recorded customer relationship and trade name intangible assets totaling 4% of total assets. The Issuer used revenue projections in valuing these intangible assets.

28. During the 2017 audit, Martin and the engagement team identified the significant judgment used in management's cash flow projections and inaccurate revenue growth rate assumptions as LSPMs with respect to the valuation of the Investment and the acquired intangible assets, respectively.

29. Martin and the engagement team determined that these LSPMs were addressed by two controls involving the corporate controller's review of cash flow projections, including revenue projections, for reasonableness.

30. However, in testing these two controls, Martin and the engagement team failed to evaluate the specific review procedures the corporate controller performed to assess the reasonableness of projected cash flows and revenue growth assumptions. Martin and the engagement team failed to evaluate whether and how the controller would follow up on items relating to management's use of significant judgment or the accuracy of revenue growth rate assumptions. Accordingly, Martin failed to ensure that the engagement team adequately tested whether the controls were designed and operating in a manner that appropriately addressed the LSPMs.[16]

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15 *See* AS 2201.42.

16 *See* AS 2201.42, .44.

E. Martin Failed to Cooperate With a Board Inspection

i. Duty to Cooperate With a Board Inspection

31. PCAOB rules require that registered public accounting firms and their associated persons "shall cooperate with the Board in the performance of any Board inspection."[17] This cooperation requirement includes an obligation not to provide misleading documents or information in connection with, or otherwise to interfere with, the Board's inspection processes.[18] An auditor provides misleading information if he or she fails to disclose that documentation presented to inspectors as having existed at the time of the audit was, in fact, subsequently altered or created.[19]

ii. Martin Failed to Disclose that a Sensitivity Analysis Provided to the PCAOB Inspectors Had Not Existed at the Time of the Audit

32. Because PwC issued its audit report on February 21, 2018, the 45 day period for PwC to complete its documentation for the 2017 audit of the Issuer ended on April 7, 2018.[20]

33. The Board selected the 2017 audit of the Issuer for inspection. The Board's Division of Registration and Inspections ("DRI") performed field work for the inspection during the week of May 21, 2018.

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17 PCAOB Rule 4006, *Duty to Cooperate with Inspectors*.

18 *See*, *e.g.*, *Kabani & Co.*, Rel. No. 34-80201, 2017 WL 947229, at *12 (SEC Mar. 10, 2017) (sustaining Board finding that respondents failed to cooperate with inspection where improper work paper alterations "interfered with the PCAOB's ability to fulfill its regulatory function of ensuring that auditors comply with their professional responsibilities"); *Dale Arnold Hotz, CPA, Jyothi Nuthulaganti Manohar, CPA, and Michael Jared Fadner, CPA*, PCAOB Rel. No. 105-2012-008, ¶ 7 (Nov. 13, 2012) (Rule 4006 "includes an obligation not to provide misleading documents or information in connection with the Board's inspection processes." (internal quotation omitted)).

19 *See*, *e.g.*, *Elliot D. Kim, CPA*, PCAOB Rel. No. 105-2018-010 (May 23, 2018) (respondent failed to cooperate with inspection when he remained silent during discussion with inspectors of document that he had improperly altered); *José Fernandez Alves*, PCAOB Rel. No. 105-2016-039 (Dec. 5, 2016) (respondent failed to cooperate when he failed to disclose during meeting with inspectors that he had learned that certain documents had been improperly altered); *Renata Coelho de Sousa Castelli*, PCAOB Rel. No. 105-2016-040 (Dec. 5, 2016) (same).

20 *See* AS 1215.15, *Audit Documentation* ("A complete and final set of audit documentation should be assembled for retention as of a date not more than 45 days after the report release date (*documentation completion date*).").

34. The engagement team's testing of the Issuer's accounting for the Acquisition, and in particular the team's testing of the customer relationship intangible asset, was an area of interest of the PCAOB inspection.

35. On May 21, 2018, a PwC audit staff member requested that PwC's Transaction Services Group perform a sensitivity analysis—"a valuation of customer relationships assuming a static growth rate of 4% in revenue"—in response to questions during the inspection. Martin was then copied on emails concerning the preparation of the analysis.

36. The next day, a member of PwC's Transaction Services Group sent the newly-created sensitivity analysis to Martin and other PwC personnel. Martin forwarded the sensitivity analysis to a PwC audit staff member, along with a note stating that it was "[o]ne more piece of support for the [Acquisition] file for tomorrow."

37. Also on May 22, 2018, Martin and other PwC personnel participated in a meeting with the PCAOB inspectors. PwC's notes of this meeting record that PwC personnel told the inspectors that a sensitivity analysis had "informed our work" with respect to the customer relationship intangible asset.

38. During the May 22 meeting, neither Martin nor any other PwC personnel disclosed that the specific sensitivity analysis shown to the inspectors had not existed during the 2017 audit, and so could not have informed their work at the time of the audit.

39. On May 24, 2018, Martin and other PwC personnel participated in another meeting with the inspectors to discuss the engagement team's testing of the Acquisition. PwC personnel provided the inspectors with a hard copy of the sensitivity analysis. Martin and her team did not provide the inspectors with an electronic copy of the sensitivity analysis; nor did they disclose that the sensitivity analysis had been created during the inspection week, and not during the 2017 audit.

40. At the end of the day on May 24, Martin and one other PwC representative attended an additional meeting with a PCAOB inspector. PwC's notes from this meeting, which were located in a spreadsheet tab labeled "High priority," indicate that the inspector requested "anyting [sic] that can show the sensitivy [sic] was done at the time of the audit." The notes do not reflect a response.

41. Martin knew or should have known that the inspector's comment reflected her understanding that PwC purported to have performed the sensitivity analysis at the time of the 2017 audit. Nonetheless, Martin did not disclose that the sensitivity analysis had, in fact, been created during the inspection, and not during the time of the 2017 audit of the Issuer.

42. Martin's acts and omissions as described above violated her duty under Rule 4006 to cooperate with the Board's inspection of the 2017 audit of the Issuer.

IV.

In view of the foregoing, and to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports, the Board determines it appropriate to impose the sanctions agreed to in Respondent's Offer. Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 105(c)(4)(B) of the Act and PCAOB Rule 5300(a)(2), Sarah C. Martin, CPA is barred from being an associated person of a registered public accounting firm, as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(i);[21]

B. Pursuant to PCAOB Rule 5302(b), Sarah C. Martin may file a petition for Board consent to associate with a registered public accounting firm after one year from the date of this Order; and

C. Pursuant to Section 105(c)(4)(D) of the Act and PCAOB Rule 5300(a)(4), the Board imposes a civil money penalty in the amount of $10,000 on Sarah C. Martin. All funds collected by the Board as a result of the assessment of these civil money penalties will be used in accordance with Section 109(c)(2) of the Act. Respondent shall pay the civil money penalty within 10 days of the issuance of this Order by (1) wire transfer in accordance with instructions furnished by Board staff; or (2) United States Postal Service money order, bank money order, certified check, or bank cashier's check (a) made payable to the Public Company Accounting Oversight Board, (b) delivered to the Office of Finance, Public Company Accounting Oversight Board, 1666 K Street, N.W., Washington D.C. 20006, and (c) submitted under a cover letter, which identifies Sarah C. Martin as a respondent in these proceedings, sets forth the title and PCAOB release number of these proceedings, and states that payment is made pursuant to this

[21] As a consequence of the bar, the provisions of Section 105(c)(7)(B) of the Act will apply with respect to Martin. Section 105(c)(7)(B) provides: "It shall be unlawful for any person that is suspended or barred from being associated with a registered public accounting firm under this subsection willfully to become or remain associated with any issuer, broker, or dealer in an accountancy or a financial management capacity, and for any issuer, broker, or dealer that knew, or in the exercise of reasonable care should have known, of such suspension or bar, to permit such an association, without the consent of the Board or the Commission."

Order, a copy of which cover letter and money order or check shall be sent to Office of the Secretary, Attention: Phoebe W. Brown, Secretary, Public Company Accounting Oversight Board, 1666 K Street, N.W., Washington D.C. 20006. ***Respondent Sarah C. Martin understands that failure to pay the civil money penalty described above may alone be grounds to deny any petition, pursuant to PCAOB Rule 5302(b), for Board consent to associate with a registered public accounting firm.***

ISSUED BY THE BOARD.

/s/ Phoebe W. Brown

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Phoebe W. Brown
Secretary

September 17, 2021