2019 Inspection B F Borgers CPA PC

(Headquartered in Lakewood, Colorado)

August 16, 2021

PCAOB

Public Company Accounting Oversight Board

<u>**THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT**</u>

PORTIONS OF THE COMPLETE REPORT ARE OMITTED FROM THIS DOCUMENT IN ORDER TO COMPLY WITH SECTIONS 104(g)(2) AND 105(b)(5)(A) OF THE SARBANES-OXLEY ACT OF 2002

PCAOB RELEASE NO. 104-2021-155A
(Includes portions of Part II of the full report that were not included in PCAOB Release No. 104-2021-155)

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2019 Inspection

During the Public Company Accounting Oversight Board ("PCAOB")'s 2019 inspection of B F Borgers CPA PC, we assessed the firm's compliance with laws, rules, and professional standards applicable to the audits of public companies.

We selected for review nine audits of issuers with fiscal years generally ending in 2018. For each issuer audit selected, we reviewed a portion of the audit. We also evaluated elements of the firm's system of quality control.

2019 Inspection Approach

In selecting issuer audits for review, we use a risk-based method of selection. We make selections based on (1) our internal evaluation of audits we believe have a heightened risk of material misstatement, including those with challenging audit areas, and (2) other risk-based characteristics, including issuer and firm considerations. In certain situations we may select all of the firm's issuer audits for review.

When we review an audit, we do not review every aspect of the audit. Rather, we generally focus our attention on audit areas we believe to be of greater complexity, areas of greater significance or with a heightened risk of material misstatement to the issuer's financial statements, and areas of recurring deficiencies. We may also select some audit areas for review in a manner designed to incorporate unpredictability.

Our selection of audits for review does not constitute a representative sample of the firm's total population of issuer audits. Additionally, our inspection findings are specific to the particular portions of the issuer audits reviewed. They are not an assessment of all of the firm's audit work nor of all of the audit procedures performed for the audits reviewed.

View the details on the scope of our inspections and our inspections procedures.

Overview of the 2019 Inspection and Historical Data by Inspection Year

The following information provides an overview of our inspection in 2019 of the firm's issuer audits as well as data from the previous inspection. We use a risk-based method to select audits for review and to identify areas on which we focus our review. Because our inspection process evolves over time, it can, and often does, focus on a different mix of audits and audit areas from inspection to inspection and firm to firm. Further, a firm's business, the applicable auditing standards, or other factors can change from the time of one inspection to the next. As a result of these variations, we caution that our inspection results are not necessarily comparable over time or among firms.

Firm Data and Audits Reviewed

	2019	2017
Firm Data		
Total issuer audit clients for which the firm was the principal auditor at the outset of the inspection procedures	80	72
Total engagement partners on issuer audit work[1]	3	3
Audits Reviewed		
Total audits reviewed[2]	9	7
Audits in which the firm was the principal auditor	9	7
Integrated audits of financial statements and internal control over financial reporting ("ICFR")	0	0
Audits with Part I.A deficiencies	8	7

If a deficiency is included in Part I.A of our report, it does not necessarily mean that the firm has not addressed the deficiency. In many cases, the firm has performed remedial actions after the issue was identified. Depending on the circumstances, remedial actions may include performing additional audit procedures, informing management of the issuer of the need for changes to the financial statements or reporting on ICFR, or taking steps to prevent reliance on prior audit reports. Our inspection may include a review, on a sample basis, of the adequacy of a firm's remedial actions, either with respect to previously

[1] The number of engagement partners on issuer audit work represents the total number of firm personnel (not necessarily limited to personnel with an ownership interest) who had primary responsibility for an issuer audit (as defined in AS 1201) during the twelve-month period preceding the outset of the inspection.

[2] The population of issuer audits from which audits are selected for review may differ from the issuer audits at the outset of the inspection procedures due to variations such as new issuer audit clients for which the firm has not yet issued an opinion or issuer audit clients lost prior to the outset of the inspection.

identified deficiencies or deficiencies identified during the current inspection. If a firm does not take appropriate actions to address deficiencies, we may criticize its system of quality control or pursue a disciplinary action.

The fact that we have included a deficiency in our report — other than those deficiencies for audits with incorrect opinions on the financial statements and/or ICFR — does not necessarily mean that the issuer's financial statements are materially misstated or that undisclosed material weaknesses in ICFR exist. It is often not possible for us to reach a conclusion on those points based on our inspection procedures and related findings because, for example, we have only the information that the auditor retained and the issuer's public disclosures. We do not have direct access to the issuer's management, underlying books and records, and other information.

Audit Areas Most Frequently Reviewed

This table reflects the audit areas we have selected most frequently for review in the 2019 inspection and the previous inspection. For the issuer audits selected for review, we selected these areas because they were generally significant to the issuer's financial statements, may have included complex issues for auditors, and/or involved complex judgments in (1) estimating and auditing the reported value of related accounts and disclosures and (2) implementing and auditing the related controls.

2019		2017	
Audit area	**Audits reviewed**	**Audit area**	**Audits reviewed**
Revenue and related accounts	9	**Revenue and related accounts**	7
Goodwill and intangible assets	5	**Cash and cash equivalents**	5
Cash and cash equivalents	4	**Equity and equity-related transactions**	4
Business combinations	3	**Goodwill and intangible assets**	2
Going concern	2	**Inventory**	2

Part I: Inspection Observations

Part I.A of our report discusses deficiencies, if any, that were of such significance that we believe the firm, at the time it issued its audit report(s), had not obtained sufficient appropriate audit evidence to support its opinion on the issuer's financial statements and/or ICFR. Part I.B discusses deficiencies, if any, that do not relate directly to the sufficiency or appropriateness of evidence the firm obtained to support its opinion(s) but nevertheless relate to instances of non-compliance with PCAOB standards or rules. Consistent with the Sarbanes-Oxley Act ("the Act"), it is the Board's assessment that nothing in Part I of this report deals with a criticism of or potential defect in the firm's quality control system. Any such criticisms or potential defects are discussed in Part II. Further, you should not infer from any Part I deficiency or combination of deficiencies that a quality control finding is identified in Part II. Section 104(g)(2) of the Act restricts us from publicly disclosing Part II deficiencies unless the firm does not address the criticisms or potential defects to the Board's satisfaction no later than 12 months after the issuance of this report.

Classification of Audits with Part I.A Deficiencies

Within Part I.A of this report, we classify each issuer audit in one of the categories discussed below based on the Part I.A deficiency or deficiencies identified in our review.

The sole purpose of this classification system is to group and present issuer audits by the number of Part I.A deficiencies we identified within the audit as well as to highlight audits with an incorrect opinion on the financial statements and/or ICFR.

Audits with an Incorrect Opinion on the Financial Statements and/or ICFR

This classification includes instances where a deficiency was identified in connection with our inspection and, as a result, an issuer's financial statements were determined to be materially misstated, and the issuer restated its financial statements. It also includes instances where a deficiency was identified in connection with our inspection and, as a result, an issuer's ICFR was determined to be ineffective, or there were additional material weaknesses that the firm did not identify, and the firm withdrew its opinion, or modified its report, on ICFR. This classification does not include instances where, unrelated to our review, an issuer restated its financial statements and/or an issuer's ICFR was determined to be ineffective. Any deficiencies identified in connection with our reviews of these audits would be included in the audits with multiple deficiencies or audits with a single deficiency classification below.

Audits with Multiple Deficiencies

This classification includes instances where multiple deficiencies were identified that related to a combination of one or more financial statement accounts, disclosures, and/or important controls in an ICFR audit.

Audits with a Single Deficiency

This classification includes instances where a single deficiency was identified that related to a financial statement account or disclosure or to an important control in an ICFR audit.

Part I.A: Audits with Unsupported Opinions

This section of our report discusses the deficiencies identified, by specific issuer audit reviewed, in the audit work supporting the firm's opinion on the issuer's financial statements.

We identify each issuer by a letter (e.g., Issuer A). Each deficiency could relate to several auditing standards, but we reference the PCAOB standard(s) that most directly relates to the requirement with which the firm did not comply.

Issuer audits are presented below within their respective deficiency classifications (as discussed previously). Within the classifications, we generally present the audits based on our assessment as to the relative significance of the identified deficiencies taking into account the significance of the financial statement accounts and/or disclosures affected, and/or the nature or extent of the deficiencies.

Audits with an Incorrect Opinion on the Financial Statements and/or ICFR

None

Audits with Multiple Deficiencies

Issuer A

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Long-Lived Assets, Segment Disclosures, Accounts Receivable,** a **Certain Asset, Investments,** and **Discontinued Operations**.

Description of the deficiencies identified

With respect to **Long-Lived Assets**:

The issuer purchased land and buildings (the "acquired property") and assumed certain legal obligations ("assumed liabilities"). The issuer engaged an external specialist to value the acquired property. The issuer valued the assumed liabilities based on the seller's estimate of costs to satisfy the obligation and certain performance guarantees.

The firm did not identify, or appropriately address, departures from GAAP related to the issuer (1) not allocating certain capitalized costs to the carrying amounts of the related components of the acquired property in conformity with FASB ASC Topic 410, *Asset Retirement and Environmental Obligations,* and (2) inappropriately disclosing all assets of the acquired property within one asset category instead of disclosing balances of major classes of depreciable assets, by nature or function, in conformity with FASB ASC Topic 360, *Property, Plant, and Equipment*. (AS 2810.30 and .31)

The firm did not test the data used by the external specialist to value the acquired property. (AS 1210.12) In addition, the firm did not evaluate the reasonableness of the assumptions developed by the external specialist to value the acquired property. (AS 2502.26 and .28)

The firm did not evaluate whether the assumed liabilities recorded by the issuer represented a reasonable estimate of their fair value. (AS 2502.26 and .28) In addition, the firm did not evaluate whether the presentation of the assumed liabilities as a non-current liability was in conformity with FASB ASC Topic 210, *Balance Sheet*. (AS 2810.30)

With respect to **Segment Disclosures**:

The firm did not identify, or appropriately address, departures from GAAP related to (1) inaccuracies in the amount of assets allocated to the issuer's segments, and (2) the issuer's omission of a disclosure related to the total amount of revenue from a customer that represented more than ten percent of revenue, as required by FASB ASC Topic 280, *Segment Reporting*. (AS 2810.30 and .31) In addition, the firm did not evaluate whether each segment disclosed by the issuer met the criteria to be considered an operating segment in conformity with FASB ASC Topic 280. (AS 2810.30 and .31)

With respect to **Accounts Receivable**:

The firm received electronic responses to its accounts receivable confirmation requests. The firm did not consider performing procedures to address the risks associated with electronic responses, such as verifying the source and contents of the confirmation responses. (AS 2310.29)

The firm's approach for substantively testing the allowance for doubtful accounts was to review and test management's process. The firm did not sufficiently evaluate the reasonableness of the allowance because it limited its procedures to (1) inquiry of management and (2) obtaining documents from the issuer related to promises from its customers to pay the amounts owed without evaluating the authenticity and reliability of those documents. (AS 2501.09, .10, and .11)

With respect to a **Certain Asset**:

The issuer identified impairment indicators related to a certain asset. The issuer engaged an external specialist to determine the asset's fair value and also relied upon its sale of the asset, through a non-monetary transaction, subsequent to year end in concluding that the asset was not impaired. The firm did not perform sufficient procedures to evaluate the issuer's conclusions. The following deficiencies were identified:

- The firm did not test the data used by the external specialist to determine the fair value of the asset. (AS 1210.12)

- The firm did not evaluate the reasonableness of assumptions used by the external specialist to determine the fair value. (AS 2502.26 and .28)

- The firm did not test the fair value of the subsequent sale of this asset. (AS 2502.26 and .28)

In addition, the firm did not evaluate whether the presentation of the asset as a current asset in the issuer's balance sheet was in conformity with FASB ASC Topic 210. (AS 2810.30)

With respect to **Investments**:

The issuer held certain non-marketable equity investments that were recorded at adjusted cost. For one of these investments, the firm did not perform sufficient procedures to evaluate the issuer's conclusion that the investment was not impaired because the firm did not (1) test the issuer's qualitative assessment and (2) test the fair value of the issuer's sale of this investment, through a non-monetary transaction, subsequent to year end, which the issuer used to support its conclusion that the investment was not impaired at year end. (AS 2501.07)

For another of these investments, the issuer concluded that the investment was not impaired based, in part, on a private placement transaction earlier in the year. The firm did not perform sufficient procedures to evaluate the issuer's conclusions that the investment was not impaired because the firm did not (1) test the issuer's qualitative assessment; (2) evaluate whether impairment indicators existed because the investee company reported a net loss for the year and its total liabilities exceeded its total assets; and (3) evaluate the value of the investee's shares at year end relative to the private placement transaction earlier in the year. (AS 2301.08)

The issuer also held an investment in an entity for which it had a majority ownership, but the entity was not consolidated due to certain qualitative considerations. The firm did not evaluate these qualitative considerations in assessing whether the issuer's accounting was in conformity with FASB ASC Topic 323, *Investments – Equity Method and Joint Ventures*. (AS 2810.30) The issuer identified impairment indicators related to this investment and engaged an external specialist to estimate its fair value. The firm did not test the data used by the external specialist to determine the fair value. (AS 1210.12) In addition, the firm did not evaluate the reasonableness of the assumptions used by the external specialist to estimate the fair value. (AS 2502.26 and .28)

With respect to **Discontinued Operations**:

The issuer indicated its intention to phase out components of its business. The firm did not evaluate whether these components should have been reported as discontinued operations in conformity with FASB ASC Subtopic 205-20, *Presentation of Financial Statements – Discontinued Operations*. (AS 2810.30 and .31)

Issuer B

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Revenue, Accounts Receivable, Business Combinations, Investments, Related Party Transactions,** and **Going Concern.**

Description of the deficiencies identified

With respect to **Revenue**:

The issuer adopted FASB Topic ASC 606, *Revenue from Contracts with Customers,* during the year under audit. The firm did not perform procedures, beyond reading an issuer-prepared memorandum, to evaluate the significant judgments made by the issuer in the application of FASB ASC Topic 606, including the appropriateness of the issuer's determination that consideration did not need to be allocated to certain performance obligations. (AS 2301.08)

In addition, the firm did not identify, or appropriately address, departures from GAAP related to the issuer's omission of disclosures related to (1) the nature of and reason for the change in accounting principle and, (2) the transition method used by the issuer, as required by FASB ASC Topic 606. (AS 2810.30 and .31)

With respect to **Accounts Receivable**:

To substantively test accounts receivable, the firm sent confirmation requests for a selection of accounts receivable that met certain criteria. The firm did not perform any procedures to test the remaining population of accounts receivable. (AS 1105.27)

With respect to **Business Combinations**:

During the year, the issuer acquired certain businesses and engaged an external specialist to estimate the fair value of certain acquired intangible assets. The firm did not test the data used by the external specialist to estimate the fair value. (AS 1210.12) In addition, the firm did not evaluate the reasonableness of assumptions used by the external specialist to estimate the fair value. (AS 2502.26 and .28)

For certain other business combinations, the firm did not evaluate the reasonableness of the estimated useful lives of the acquired intangible assets. (AS 2501.07)

With respect to **Investments**:

The issuer reported an equity-method investment in an investee whose fiscal year end was six months earlier than the issuer's. The firm did not test any transactions, or the investee's financial information, for the six-month period between the investee's and the issuer's fiscal year ends. (AS 2503.28) In addition, the firm did not test the percentage of ownership in the investee at year end. (AS 2301.08)

With respect to **Related Party Transactions**:

The firm did not evaluate whether the issuer had properly identified its related parties and relationships and transactions with related parties, including testing the accuracy and completeness of the related parties and relationships and transactions with related parties identified by the issuer. Further, the firm did not evaluate whether related party transactions were properly accounted for and disclosed in the issuer's financial statements. (AS 2410.14 and .17)

With respect to **Going Concern**:

During the year under audit, the firm identified conditions and events that caused it to believe there could be substantial doubt about the issuer's ability to continue as a going concern for a reasonable period of time and concluded that the substantial doubt was alleviated. The firm did not sufficiently evaluate management's plans, because it did not test the prospective financial information, including the issuer's ability to carry out a significant planned reduction in operating expenditures, which was significant to overcoming the adverse conditions and events. (AS 2415.03, .08, and .09)

Issuer C

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Revenue and Accounts Receivable, Allowance for Doubtful Accounts, Business Combinations, Goodwill and Intangible Assets,** and **Comparability of Financial Statements**.

Description of the deficiencies identified

With respect to **Revenue and Accounts Receivable**:

The firm's approach to testing revenue included testing selected revenue transactions for one type of revenue and contracts for another type of revenue. For the selected transactions and one of the contracts selected for testing, the firm did not evaluate the appropriateness of revenue recognized. (AS 2301.08)

The firm selected for confirmation key items related to certain revenue and accounts receivable transactions. The following deficiencies were identified:

- The firm received electronic responses to its confirmation requests. The firm did not consider performing procedures to address the risks associated with electronic responses, such as verifying the source and contents of the confirmation responses. (AS 2310.29)

- The firm did not perform alternative procedures for positive confirmation requests for which it did not receive a response. (AS 2310.31)

- The firm did not evaluate the nature of exceptions in returned confirmations. (AS 2310.33)

- The firm did not perform any procedures to test the remaining population of accounts receivable that was not included in the confirmation selections. (AS 1105.27)

With respect to the **Allowance for Doubtful Accounts**:

The firm's approach for substantively testing the allowance for doubtful accounts was to review and test management's process. The firm did not sufficiently evaluate the reasonableness of the allowance because the firm did not perform procedures to test the assumptions the issuer used to determine the allowance. (AS 2501.09, .10, and .11) In addition, the firm did not test the accuracy and completeness of data the issuer used to determine the allowance. (AS 1105.10; AS 2501.11)

With respect to **Business Combinations**:

During the year, the issuer acquired certain businesses. The firm did not perform audit procedures, beyond reading the issuer-prepared memoranda, merger agreements, and related acquisition documents, to understand the issuer's process in determining fair value measurements and disclosures, including the data and assumptions that were used in the analyses, in order to plan the nature, timing, and extent of the audit procedures. (AS 2502.11) In addition, the firm did not test the fair values of the acquired intangible assets and test the measurement of goodwill. (AS 2502.26 and .28) The firm also did not test the presentation and disclosure of certain acquisitions in the notes to the financial statements. (AS 2502.43)

With respect to **Goodwill and Intangible Assets**:

During the prior year, the issuer acquired a business and recorded both goodwill and intangible assets. During the year under audit, the issuer performed an impairment analysis as a result of the discovery of misrepresentations the seller made, and recorded an impairment loss for that goodwill. The firm did not identify that certain of these misrepresentations existed at the date of the audit report for the prior year and evaluate whether appropriate revisions to the prior year's financial statements should have been disclosed in the financial statements of the year under audit. (AS 2905.04, .05, and .06)

The firm did not evaluate the reasonableness of assumptions used in the issuer's goodwill impairment analysis. (AS 2502.26 and .28) In addition, the firm did not evaluate the reasonableness of the issuer's conclusion that its other intangible assets related to this reporting unit were not also impaired. (AS 2501.07; AS 2810.03)

With respect to **Comparability of Financial Statements**:

During the year under audit, the issuer disclosed that it corrected certain immaterial errors contained in its prior year financial statements. The firm did not evaluate the issuer's conclusion that these errors were immaterial to each affected year and whether the comparability of the financial statements between periods was materially affected by the adjustments that were made to previously issued financial statements. (AS 2820.02)

Issuer D

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Goodwill, Accounts Receivable,** and **Going Concern**.

Description of the deficiencies identified

With respect to **Goodwill**:

In its annual goodwill impairment test, the issuer compared the fair value of a reporting unit to the recorded amount of goodwill. The firm did not identify, and evaluate the significance to the issuer's financial statements of, a departure from GAAP related to the issuer's failure to compare the fair value of the reporting unit to its carrying amount, including goodwill, in conformity with FASB ASC Topic 350, *Intangibles – Goodwill and Other*. (AS 2810.30)

The firm did not perform any procedures to evaluate the reasonableness of certain assumptions used by the issuer to estimate the fair value of the reporting unit. (AS 2502.26 and .28)

With respect to **Accounts Receivable**:

To test accounts receivable, the firm sent confirmation requests, either by mail or electronic mail, to a selection of the issuer's customers that met certain criteria. The following deficiencies were identified:

- The firm received electronic responses to certain of its confirmation requests. The firm did not consider performing procedures to address the risks associated with electronic responses, such as verifying the source and contents of the confirmation responses. (AS 2310.29)
- The firm did not perform alternative procedures for positive confirmation requests for which it did not receive a response. (AS 2310.31)
- The firm did not evaluate the nature of exceptions in returned confirmations. (AS 2310.33)
- The firm did not perform any procedures to test the remaining population of accounts receivable that was not included in the confirmation selections. (AS 1105.27)

The firm's approach for substantively testing the allowance for doubtful accounts was to review and test management's process. The firm did not sufficiently evaluate the reasonableness of the allowance because the firm did not perform procedures to test the assumptions the issuer used to determine the allowance. (AS 2501.09, .10, and .11) In addition, the firm did not test the accuracy and completeness of data the issuer used to determine the allowance. (AS 1105.10; AS 2501.11)

With respect to **Going Concern**:

During the year under audit, the firm identified conditions and events that caused it to believe there could be substantial doubt about the issuer's ability to continue as a going concern for a reasonable period of time and concluded that the substantial doubt was alleviated. The firm did not sufficiently evaluate management's plans, because it did not assess the likelihood that the issuer could obtain additional funding. (AS 2415.03 and .08)

Issuer E

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Revenue** and **Goodwill and Intangible Assets**.

Description of the deficiencies identified

With respect to **Revenue**:

The issuer recognized revenue using certain inputs and assumptions to measure its progress toward the completion of its performance obligations. The firm's approach for substantively testing the estimate of progress toward completion was to review and test management's process. The firm did not sufficiently evaluate the reasonableness of this estimate because the firm did not test the accuracy and completeness of the inputs the issuer used to determine the estimate. (AS 1105.10; AS 2501.11) In addition, the firm did not perform procedures to test the assumptions the issuer used to determine the estimate. (AS 2501.09, .10, and .11)

With respect to **Goodwill and Intangible Assets**:

The issuer reported goodwill and/or intangible assets in certain reporting units. The issuer estimated the fair value of certain of these reporting units to assess whether there was a potential impairment. The following deficiencies were identified:

- With respect to one reporting unit, the firm did not identify, and evaluate the significance to the issuer's financial statement of, a departure from GAAP related to the issuer combining indefinite-lived intangible assets with goodwill and finite-lived assets when performing its impairment testing, which is not in conformity with FASB ASC Topic 350. (AS 2810.30) In addition, the firm did not evaluate the reasonableness of significant assumptions used by the issuer in its estimate of fair value. (AS 2502.26 and .28)

- With respect to another reporting unit, the firm did not evaluate the reasonableness of the assumptions used by the issuer in its estimate of the fair value. (AS 2502.26 and .28)

- With respect to a third reporting unit, the firm did not perform any procedures to evaluate whether the issuer tested goodwill for impairment. (AS 2301.08)

Issuer F

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Revenue, Accounts Receivable**, and the **Allowance for Doubtful Accounts**.

Description of the deficiencies identified

With respect to **Revenue**:

The firm selected certain revenue contracts for testing. The firm did not identify and test whether all relevant performance obligations for revenue recognition had been met for those contracts selected for testing. (AS 2301.08)

For one type of revenue, the firm used a sampling tool to determine the sample size for testing, but only tested a subset of the sample. (AS 2315.25) In addition, the firm sent confirmation requests to a sample of customers, and a majority of the confirmation responses received were provided to the firm after having been initially received by the issuer. The firm did not maintain control over the confirmation requests and responses through direct communication between the firm and the intended recipients of the confirmation requests. (AS 2310.28)

For another type of revenue, the firm selected transactions for testing that met certain criteria. The firm did not perform any procedures to test the remaining population that was not included in the selections. (AS 1105.27) In addition, the firm did not perform any substantive procedures to test, or in the alternative, test controls over, the accuracy and completeness of issuer-generated invoices used in the firm's testing of this type of revenue. (AS 1105.10)

With respect to **Accounts Receivable**:

The firm received electronic responses to its accounts receivable confirmation requests. The firm did not consider performing procedures to address the risks associated with electronic responses, such as verifying the source and contents of the confirmation responses. (AS 2310.29)

With respect to the **Allowance for Doubtful Accounts**:

The firm's approach for substantively testing the allowance for doubtful accounts was to review subsequent transactions. The firm did not sufficiently evaluate the reasonableness of the allowance because the firm limited its procedures to reviewing cash collections subsequent to year end for one customer's accounts receivable balance. (AS 2501.09, .10, and .13)

Issuer G – Health Care

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Convertible Debt** and **Goodwill**.

Description of the deficiencies identified

With respect to **Convertible Debt**:

The firm did not identify, and evaluate the significance to the issuer's financial statements of, a departure from GAAP related to the conversion features of certain convertible notes that should have been accounted for as either beneficial conversion features in conformity with FASB ASC Subtopic 470-20, *Debt – Debt with Conversion and Other Options*, or as embedded derivatives in conformity with FASB ASC Topic 815, *Derivatives and Hedging*. (AS 2810.30)

The firm identified errors related to certain of the issuer's convertible notes. The firm did not evaluate whether the uncorrected misstatements were material, individually or in combination with other misstatements. (AS 2810.17)

With respect to **Goodwill**:

The issuer performed a qualitative assessment of goodwill impairment and used a recent fair value calculation prepared by an external specialist in concluding to not perform a quantitative goodwill impairment test. The firm did not sufficiently evaluate whether the issuer considered certain relevant events or changes in circumstances in conformity with FASB ASC Subtopic 350-20, *Intangibles – Goodwill and Other – Goodwill*, including the issuer's operating losses, negative working capital, and substantial doubt about the issuer's ability to continue as a going concern. (AS 2810.03 and .30) In addition, the firm did not perform any procedures, beyond inquiry of the external specialist, to (1) test the data, (2) evaluate the reasonableness of assumptions, and (3) evaluate the relevance and reliability of information the specialist used in the recent fair value calculation that the firm used to support its evaluation of the issuer's qualitative assessment. (AS 2501.09, .10, and .11)

Audits with a Single Deficiency

Issuer H

Type of audit and related area affected

In our review, we identified a deficiency in the financial statement audit related to **Inventory**.

Description of the deficiency identified

The firm performed inventory observations at an interim date and performed roll-forward procedures for the period from the interim date to year end. The firm did not perform any substantive procedures to test, or in the alternative, test controls over, the accuracy and completeness of information the firm used in performing the roll-forward procedures. (AS 1105.10)

Part I.B: Other Instances of Non-Compliance with PCAOB Standards or Rules

This section of our report discusses any deficiencies we identified that do not relate directly to the sufficiency or appropriateness of evidence the firm obtained to support its opinion(s) but nevertheless relate to instances of non-compliance with PCAOB standards or rules. When we review an audit, we do not review every aspect of the audit. As a result, the areas below were not necessarily reviewed on every audit. In some cases, we assess the firm's compliance with specific PCAOB standards or rules on other audits that were not otherwise selected for review and may include instances of non-compliance below.

The deficiencies below are presented in numerical order based on the PCAOB standard or rule with which the firm did not comply. We identified the following deficiencies:

- In five of nine audits reviewed, the firm did not include all of the required information in its engagement completion document. In these instances, the firm was non-compliant with AS 1215, *Audit Documentation*.

- In five of nine audits reviewed, the firm did not make certain required communications to the issuer's audit committee, or equivalent, related to the significant risks identified through its risk assessment procedures. In these instances, the firm was non-compliant with AS 1301, *Communications with Audit Committees*.

- In two of three audits reviewed where one or more other accounting firms participated in the firm's audit, the firm did not make certain required communications to the issuer's audit committee, or equivalent, related to the names, locations, and planned responsibilities of other independent public accounting firms that performed audit procedures in the audit. In these instances, the firm was non-compliant with AS 1301, *Communications with Audit Committees*.

- In one of nine audits reviewed, the firm did not make certain required communications to the issuer's audit committee related to matters regarding the firm's evaluation of the issuer's ability to continue as a going concern. In this instance, the firm was non-compliant with AS 1301, *Communications with Audit Committees*.

- In one of nine audits reviewed, the firm did not make a required communication to the issuer's audit committee related to an overview of the overall audit strategy, including timing of the audit. In this instance, the firm was non-compliant with AS 1301, *Communications with Audit Committees*.

- In one of nine audits reviewed, the firm did not make a required communication to the issuer's audit committee related to the issuer's change in a significant accounting policy or practice during the year. In this instance, the firm was non-compliant with AS 1301, *Communications with Audit Committees*.

- In one of nine audits reviewed, the firm did not make any of the required communications to the issuer's audit committee equivalent. In this instance, the firm was non-compliant with AS 1301, *Communications with Audit Committees*.

- In one of nine audits reviewed, the firm did not communicate to the audit committee the firm's evaluation of the issuer's identification, accounting for, and disclosure of transactions with certain related parties. In this instance, the firm was non-compliant with AS 2410, *Related Parties*.

- In one of nine audits reviewed, the firm's audit report contained inaccurate information for the year the firm began serving consecutively as the company's auditor. In this instance, the firm was non-compliant with AS 3101, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion.*

- In five of nine audits reviewed, the firm's audit report did not include explanatory language about the firm's responsibilities with respect to ICFR in a non-integrated audit. In these instances, the firm was non-compliant with AS 3105, *Departures from Unqualified Opinions and Other Reporting Circumstances*.

- In two of three audits reviewed where one or more other accounting firms participated in the firm's audit, the firm's report on Form AP omitted information related to the participation in the audits by other accounting firms. In addition, in two of the three audits reviewed where one or more other accounting firms participated in the firm's audit, the firm did not (1) use a reasonable method to estimate the extent of participation in the audit by one or more other accounting firms, and (2) document in its files the computation of total hours and the method used to estimate hours. In these instances, the firm was non-compliant with PCAOB Rule 3211, *Auditor Reporting of Certain Audit Participants,* and AS 1215, *Audit Documentation*.

Part II: Observations Related To Quality Control

Part II of our report discusses criticisms of, and potential defects in, the firm's system of quality control.

Deficiencies are included in Part II if an analysis of the inspection results, including the results of the reviews of individual audits, indicates that the firm's system of quality control does not provide reasonable assurance that firm personnel will comply with applicable professional standards and requirements. Generally, the report's description of quality control criticisms is based on observations from our inspection procedures.

Any changes or improvements to its system of quality control that the firm may have brought to the Board's attention may not be reflected in this report, but are taken into account during the Board's assessment of whether the firm has satisfactorily addressed the quality control criticisms or defects no later than 12 months after the issuance of this report.

Criticisms of, and potential defects in, the firm's system of quality control, to the extent any are identified, are nonpublic when the reports are issued. If a firm does not address to the Board's satisfaction any criticism of, or potential defect in, the firm's system of quality control within 12 months after the issuance of our report, any such deficiency will be made public.

A. Firm Management's Approach to Quality Control

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the firm's personnel will comply with PCAOB standards in the firm's issuer audit practice. (QC 20.03, .04, .13, and .15)

In a significant portion of the firm's audit work reviewed in this inspection, the inspection team identified deficiencies in the performance of the work, including not identifying and appropriately addressing departures from GAAP in five audits[3] included in Part I.A. The firm should evaluate whether its policies and procedures provide reasonable assurance that it:

- Undertakes only those engagements that it can reasonably expect to complete with professional competence; and

- Assigns work on those engagements to persons who have the technical training and proficiency required in the circumstances, taking into consideration competing time demands on the firm's personnel when assigning individuals to lead issuer audits.

Identifying the underlying causes for the poor inspection results may assist the firm in assessing the need for changes or enhancements to its system of quality control. The firm should implement changes in its policies and procedures necessary to provide reasonable assurance that its personnel comply with the professional standards applicable to its issuer audit practice.

B. Testing Estimates, Including Fair Value Measurements

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the work performed by the firm's personnel to evaluate significant assumptions or data

[3] Issuers A, B, D, E, and G

underlying accounting estimates will meet the requirements of AS 1105, AS 1210, AS 2501, and AS 2502. (QC 20.03 and .17)

In seven audits,[4] all of which are included in Part I.A, the inspection team identified deficiencies related to the firm's evaluation of the reasonableness of one or more estimates, including fair value measurements.

C. Testing Revenue

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the work performed by the firm's personnel to test revenue will meet the requirements of AS 2301 and AS 2501. (QC 20.03 and .17)

In four audits,[5] all of which are included in Part I.A, the inspection team identified deficiencies related to the firm's substantive testing of revenue.

D. Selecting Specific Items to Test in a Population

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the work performed by the firm's personnel when selecting specific items to test will meet the requirements of AS 1105. (QC 20.03 and .17)

In four audits,[6] all of which are included in Part I.A, the inspection team identified deficiencies related to the firm selecting specific items to test and not performing any procedures to address the remaining population.

E. Use of Confirmations

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the work performed by the firm's personnel when obtaining and evaluating confirmations will meet the requirements of AS 2310. (QC 20.03 and .17)

In four audits,[7] all of which are included in Part I.A, the inspection team identified deficiencies related to the firm's use of confirmations, including addressing the risks associated with electronic responses, performing alternative procedures for non-responses, and evaluating exceptions in the responses.

F. Evaluating an Entity's Ability to Continue as a Going Concern

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the work performed by the firm's personnel when evaluating whether there is substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time will meet the requirements of AS 2415. (QC 20.03 and .17)

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4 Issuers A, B, C, D, E, F, and G
5 Issuers B, C, E, and F
6 Issuers B, C, D, and F
7 Issuers A, C, D, and F

In two audits,[8] both of which are included in Part I.A, the inspection team identified deficiencies related to the firm's evaluation of whether there is substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time.

G. Reliance on Data or Reports

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the work performed by the firm's personnel to establish a basis for reliance on data and reports will meet the requirements of AS 1105. (QC 20.03 and .17)

In two audits,[9] both of which are included in Part I.A, the inspection team identified deficiencies related to the firm's testing of, or in the alternative, identifying and testing controls over, the accuracy and completeness of certain data and/or reports that the firm used in its substantive testing.

H. Communications with Audit Committees

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the firm's personnel will comply with the requirements of AS 1301 and AS 2410*.* (QC 20.03 and .17)

In six audits,[10] the firm did not make certain required communications to the issuer's audit committee. In five audits,[11] the firm did not communicate to the issuer's audit committee, or equivalent, all significant risks identified through the firm's risk assessment procedures. In two audits,[12] the firm did not communicate to the issuer's audit committee the names, locations, and planned responsibilities of certain other independent public accounting firms that performed audit procedures in the audit. In one audit,[13] the firm did not communicate to the issuer's audit committee matters relating to the firm's evaluation of the issuer's ability to continue as a going concern; an overview of the overall audit strategy, including timing of the audit; and a change in the revenue recognition accounting principle during the year. In one audit,[14] the firm did not communicate to the audit committee the firm's evaluation of the issuer's identification of, accounting for, and disclosure of transactions with certain related parties. In one audit,[15] the firm did not make any of the required communications to the issuer's audit committee equivalent.

I. Fraud Procedures

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the firm's personnel will perform all of the procedures necessary to comply with AS 2401. (QC 20.03 and .17)

8 Issuers B and D
9 Issuers F and H
10 Issuers A, B, E, F, G, and I
11 Issuers A, B, F, G and I
12 Issuers A and F
13 Issuer B
14 Issuer E
15 Issuer I

In four audits,[16] the firm did not test the completeness of the population from which it selected journal entries for testing. In three audits,[17] the firm did not consider the effectiveness of controls, including identified material weaknesses and/or control deficiencies related to inadequate segregation of duties, when determining the nature, timing, and extent of the testing of journal entries. In one audit,[18] the firm did not identify characteristics of fraudulent entries or adjustments and select journal entries with those characteristics for testing. In one audit,[19] the firm did not test the issuer's adjustments made in the preparation of its consolidated financial statements.

J. Compliance with Certain Audit Documentation Requirements

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the firm's personnel will comply with the firm's policy on audit documentation; this policy is consistent with the requirements of AS 1215. (QC 20.03 and .17)

In five audits,[20] the firm did not include all of the required information in the engagement completion document.

K. Engagement Quality Review

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the review procedures performed by the firm's EQR partners will meet the requirements of AS 1220. (QC 20.03 and .17)

The firm did not establish appropriate quality control policies and procedures related to engagement quality reviews, because the nature of certain procedures defined in the firm's quality control policies were inconsistent with the requirements of AS 1220. In addition, the firm's policy referenced generally accepted auditing standards instead of PCAOB standards.

In eight audits,[21] the EQR partner did not appear to possess the level of knowledge and competence related to accounting, auditing, and financial reporting required to serve as the engagement quality reviewer. AS 1220 requires that a firm use an engagement quality reviewer who possesses the level of knowledge and competence required to serve as the engagement partner on the audit. The firm appears to have had no basis for judging whether the individual it retained to perform the engagement quality reviews had such knowledge and competence.

In eight audits,[22] seven[23] of which are included in Part I.A and five[24] of which are included in Part I.B, the inspection team identified one or more deficiencies in an area that the EQR partner was required to evaluate. In six of the audits included in Part I.A,[25] the EQR partner did not identify a deficiency in an area of significant risk, including in some cases a fraud risk. In the five audits included in Part I.B, the EQR

16 Issuers C, D, E, and F
17 Issuers C, D, and F
18 Issuer D
19 Issuer C
20 Issuers A, B, C, D, and F
21 Issuers A, B, C, D, E, F, H, and I
22 Issuers A, B, C, D, E, F, G, and I
23 Issuers A, B, C, D, E, F, and G
24 Issuers B, C, D, E, and I
25 Issuers A, B, C, D, E, and F

partner did not identify a deficiency in the audit report. In addition, in three audits,[26] the firm's work papers did not include sufficient information to enable an experienced auditor, having no previous connection with the engagement, to identify all the documents reviewed by, or otherwise to understand all the procedures performed by, the EQR partner.

L. Audit Reports

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that audit reports issued by the firm will meet the requirements of AS 3101 and AS 3105. (QC 20.03 and .17)

In one audit,[27] the firm's statement in the audit report regarding the year the firm began serving consecutively as the company's auditor was inconsistent with the year the firm signed the initial engagement letter.

In five audits,[28] the firm did not include the following explanatory language in its report on the issuer's financial statements:

- The company is not required to have, nor was the auditor engaged to perform, an audit of its ICFR;
- As part of the audit, the auditor is required to obtain an understanding of ICFR but not for the purpose of expressing an opinion on the effectiveness of the company's ICFR; and
- The auditor expresses no such opinion.

M. Auditor Reporting of Certain Audit Participants

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the firm's personnel will comply with PCAOB Rule 3211 and AS 1215*.* (QC 20.03 and .17)

In two audits,[29] where one or more other accounting firms participated in the firm's audit, the firm's report on Form AP did not include information related to the participation in the audits by the other accounting firms. In addition, in two audits,[30] where one or more other accounting firms participated in the firm's audit, the firm did not (1) use a reasonable method to estimate the extent of participation in the audit by one or more other accounting firms, and (2) document in its files the computation of total hours and the method used to estimate hours.

N. State Practice Qualification Requirements

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the firm will comply with relevant requirements to practice in a jurisdiction. (QC 20.17)

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26 Issuers A, D, and F
27 Issuer B
28 Issuers B, C, D, E, and I
29 Issuers A and F
30 Issuers A and H

The inspection team observed that the firm had performed audits of the financial statements of five issuers[31] whose principal executive offices were located in states that required either registration or licensure with the state as a prerequisite to performing audits in the state, or audits of entities with home offices located in the state. The firm was not registered or licensed with these states.

O. Independence

The inspection results indicate that the firm's system of quality control does not provide reasonable assurance that the firm and its personnel will comply with independence-related regulatory requirements. (QC 20.04, .09, and .10)

* * * * [I]n two audits,[32] the firm appeared not to have satisfied certain applicable independence-related regulatory requirements.

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31 Issuers A, D, E, F, and I

32 Issuers D and F

Appendix A: Firm’s Response to the Draft Inspection Report

Pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(a), the Board provided the firm an opportunity to review and comment on a draft of this report. The firm did not provide a timely written response.