

# Division of Enforcement and Investigations Update

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Division of Enforcement and Investigations

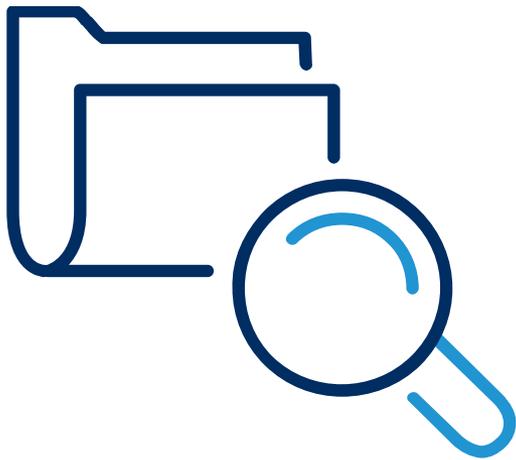
October 19, 2020

# DISCLAIMER

Any views expressed are my own and do not necessarily reflect the views of the Board as a whole, any individual Board Members, or other staff.

# DIVISION OF ENFORCEMENT & INVESTIGATIONS

What do we do.....



# AGENDA

- Today I would like to discuss:
  - Enforcement Program outlook and 2019 statistics
  - 2019 activities in certain priority or focus areas
  - Other notable enforcement areas
  - Selected recent settled matters involving significant audit standards violations
  - Extraordinary cooperation credit
  - Termination of bars

# PROGRAM OUTLOOK

- The DEI continues to prioritize:
  - Investigations involving significant audit violations presenting risks to investors
  - Matters threatening or eroding the integrity of the Board's regulatory oversight process
  - Audit matters relating to significant independence violations
- The DEI is also focusing on:
  - Matters relating to deficiencies in firm quality control policies and procedures
  - Audit matters relating to new and evolving issues (*e.g.*, cryptocurrency or cannabis)

# COORDINATION WITH THE SEC



- PCAOB may share information with the SEC, DOJ, and other agencies enumerated in the Act
- Coordination with SEC Enforcement is standard practice
  - Parallel investigations: PCAOB investigates auditor conduct; SEC investigates public company, its management, and others
- PCAOB may defer its auditor investigation to the SEC or vice versa
- PCAOB seeks to avoid duplication of effort

# PROGRAM STATISTICS FOR 2019 - OVERVIEW

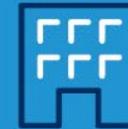
## Overview of Published Enforcement Orders



**30 settled**  
disciplinary  
orders issued



**27 individuals**  
sanctioned



**19 firms**  
sanctioned



**17 orders** involving  
U.S. auditors

**13 orders** involving  
non-U.S. auditors

**13 orders** involving the  
six largest global accounting  
firm networks

**17 orders** involving  
smaller accounting firms

# PROGRAM STATISTICS FOR 2019 - SANCTIONS

## *Sanctions Imposed*



**4 firms'**  
registrations revoked



**12 firms** required to improve their  
quality control policies and procedures



**23 auditors**  
barred or suspended

**14 auditors** required to attend  
continuing professional education courses



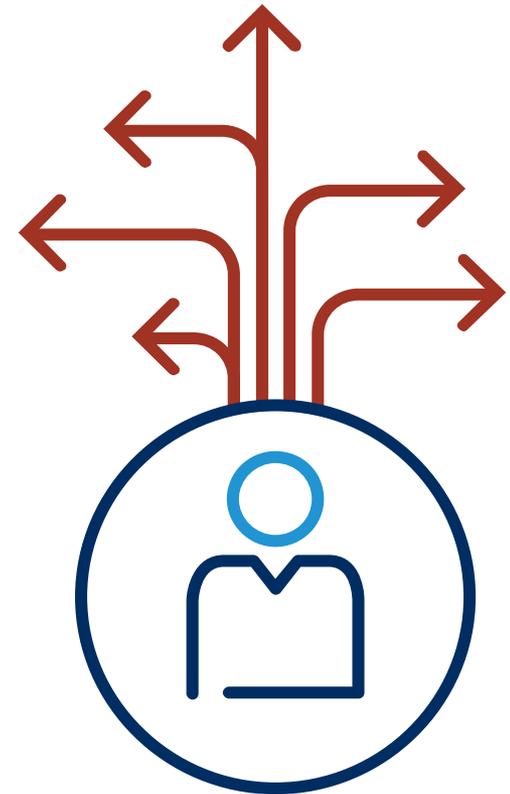
**6 auditors** restricted from acting in certain capacities  
(e.g., engagement partner, engagement quality reviewer, or in a  
quality control role)

# PROGRAM STATISTICS FOR 2019

- In the several years prior to 2019, the Board has imposed sanctions for violations of
  - Attestation Standard No. 1, Examination Engagements Regarding Compliance Reports of Brokers and Dealers, and
  - Attestation Standard No. 2, Review Engagements Regarding Exemption Reports of Brokers and Dealers
- There were **no** settled matters involving attestation standards in 2019

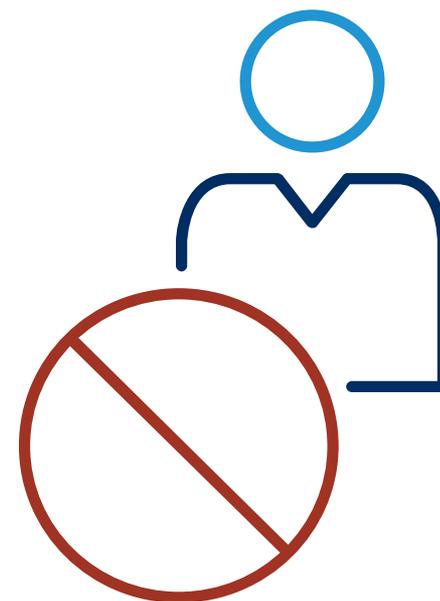
# RANGE OF POSSIBLE SANCTIONS

- In a disciplinary proceeding, the Board may:
  - impose a civil monetary penalty
  - suspend or permanently bar an individual from association with a registered public accounting firm
  - temporarily or permanently revoke a firm's registration
  - temporarily or permanently limit the activities, functions, or operations of a firm or person
  - require undertakings, such as additional professional education or training, changes to policies
  - appoint an independent monitor or consultant
  - impose a censure, and/or any other sanction per Board rules



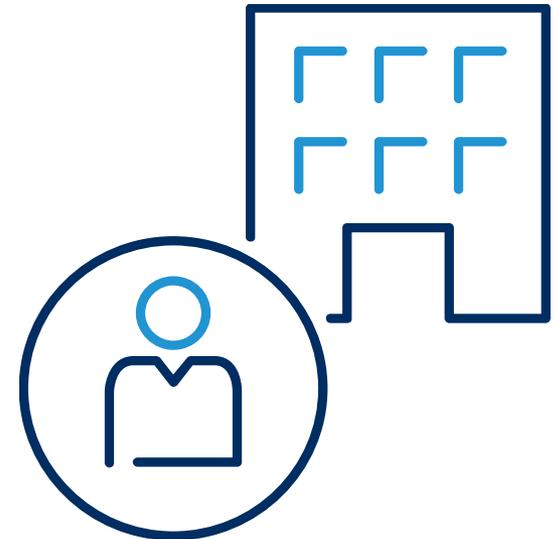
# EFFECT OF SUSPENSIONS AND BARS

- It is unlawful for any person that is suspended or barred to become or remain associated with any registered firm or with any issuer, broker, or dealer in an accountancy or a financial management capacity
  - *See Section 105(c)(7) of the Sarbanes-Oxley Act of 2002, as amended; PCAOB Rule 5301*
- It is unlawful for any registered firm, issuer, broker, or dealer that knew, or, in the exercise of reasonable care should have known, that a person is suspended or barred from association to permit such association
  - *See Section 105(c)(7) of the Sarbanes-Oxley Act of 2002, as amended; PCAOB Rule 5301*



# ASSOCIATION WITH A REGISTERED FIRM

- An individual associates with a registered firm if he or she, in connection with the preparation or issuance of any audit report:
  - Shares in the profits of, or receives compensation in any other form from, that firm; or
  - Participates as agent or otherwise on behalf of such accounting firm in any activity of that firm
    - *See Section 2(a)(9) of the Sarbanes-Oxley Act of 2002, as amended; PCAOB Rule 5301; Rules on Investigations and Adjudications, PCAOB Release No. 2003-015 (Sept. 29 2003), at A2-80-81*



# ***IN THE MATTERS OF PRITCHETT, SILER & HARDY, P.C. AND DOUGLAS W. CHILD, CPA; GRANT L. HARDY, CPA***

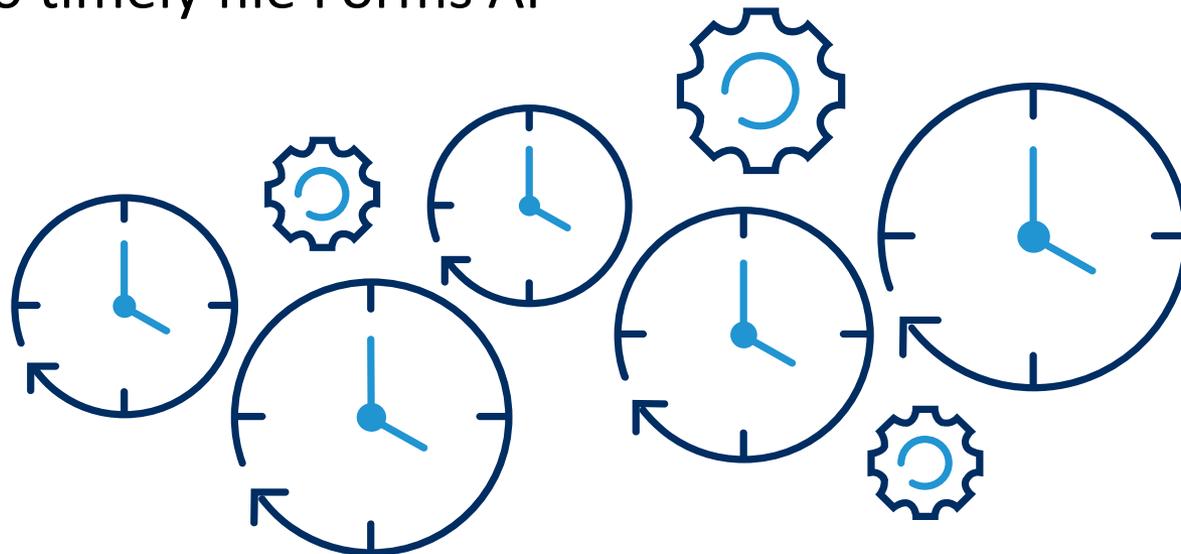
- These settled orders were issued June 5, 2019
- The firm, **PSH**, improperly permitted barred and suspended individuals to associate with the firm; and its partner responsible for issuer audits, **Child**, directly and substantially contributed to PSH's violations
  - In 2015, two individuals, **Morrill** and **Hardy**, received sanctions in a prior settlement with the Board (*In the Matter of Morrill & Associates, et al.* – Jan. 12, 2015)
    - **Morrill** was barred, but he remained a partner with Child in another, unregistered firm through which he continued to perform all of the audit work for PSH's issuer clients
    - **Hardy** was suspended and remained a partner at PSH to oversee its private audit practice. But, he nonetheless had continuing involvement in PSH's issuer audits

# *IN THE MATTERS OF PRITCHETT, SILER & HARDY, P.C. AND DOUGLAS W. CHILD, CPA; GRANT L. HARDY, CPA*

- As a result of Morrill's and Hardy's continuing association with a registered firm while under sanction
  - **PSH, Child** and **Hardy** were censured
  - **PSH's** registration was revoked
  - **Child** was barred, with the right to reapply after two years and a one-year limitation on activities after readmission
  - **Hardy** was barred, with the right to reapply after one year
- **Morrill** remains barred

# FORM AP – TIMELY FILINGS

- PCAOB Rule 3211 requires timely filing of Forms AP with the Board:
  - Within 10 days after first filing of an audit report in a registration statement with the Securities and Exchange Commission
  - Within 35 days after first filing of an audit report in other documents filed with the Commission
- During 2019, the Board has entered into **two** settlements involving failure to timely file Forms AP



# FORM AP – TIMELY FILINGS

- In one matter, sanctions were imposed for failures to timely file Forms AP, in addition to audit failures involving the performance of the firm's audits (*In the Matter of Jeffrey T. Gross Ltd. and Jeffrey T. Gross, CPA* – July 23, 2019)
- In another matter, *WDM Chartered Professional Accountants*, sanctions were imposed on March 19, 2019, solely for untimely filing of Forms AP
  - WDM failed to file an overdue Form AP for an issuer, even after it had been brought to the firm's attention during a Board Inspection, and then failed to file a subsequent Form AP for the following year's audit
  - The firm was censured, received a \$2,500 civil monetary penalty, and agreed to undertake training and review and/or supplement its policies and procedures

# MATTERS RELATING TO VIOLATIONS OF ICFR AUDITING STANDARDS

- In 2019, **three** matters involving violations of ICFR auditing standards were settled
  - *In the Matter of Timothy M. Kosiek* – April 26, 2019
    - Will be discussed later in this presentation
  - *In the Matter of Richard H. Huff, Jr., CPA* – Feb. 26, 2019, involved failures to assess the design effectiveness of certain key controls in a significant audit area
  - *In the Matter of William Trainor, CPA*

# *IN THE MATTER OF WILLIAM TRAINOR, CPA –* **JUNE 4, 2019**

- Trainor, a former EY partner, was sanctioned for inadequate evaluation for Forest Oil’s 2013 ICFR; and for failing to obtain sufficient appropriate audit evidence to support its 2013 financial statements
  - Based on his preliminary judgments, Trainor initially planned the audit for no material weaknesses in ICFR and with substantial reliance on internal controls
  - In the course of its procedures, the engagement team identified pervasive deficiencies in Forest Oil’s general IT controls
  - *Late in the audit*, he tried to overcome these deficiencies by identifying compensating controls, but those identified didn’t fully compensate
    - Notwithstanding, he authorized the issuance of effective ICFR, and unqualified financial statement, opinions

# ***IN THE MATTER OF WILLIAM TRAINOR, CPA – JUNE 4, 2019***

- He also improperly relied on controls in his audit that did not effectively address misstatement risks he had identified
- After issues with Trainor's evaluation of Forest Oil's ICFR were raised in a PCAOB inspection, management reevaluated its assessment of ICFR, and EY withdrew its 2013 ICFR opinion
- In a settlement reached after non-public proceedings had been instituted
  - Trainor was censured, received a civil monetary penalty of \$25,000 and a two year restriction on his roles in audits, and was barred concurrently, with the right to reapply after one year

# MATTERS RELATING TO DEFICIENCIES IN FIRM QUALITY CONTROLS

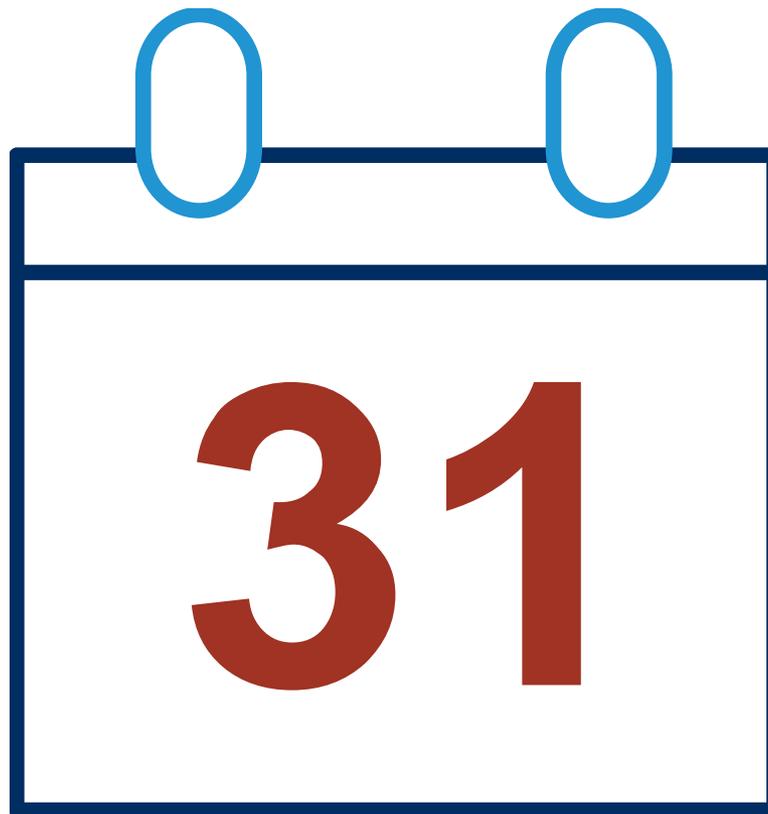
- Since at least 2019, the DEI has focused on matters relating to deficiencies in firms' quality control policies and procedures
  - Firms have responsibilities to ensure its personnel comply with the professional standards applicable to its accounting and auditing practice
  - A system of quality control provides firms with reasonable assurance that their personnel comply with applicable professional standards and the firm's standards of quality
- During 2019, the Board settled matters involving QC standards violations with **10** U.S. or International firms
- These violations were related to QC issues concerning:
  - Maintenance of appropriate audit documentation
  - Independence of issuer audit clients
  - Audits' compliance with standards
  - Association of persons with firms

# MATTERS RELATING TO DEFICIENCIES IN FIRM QUALITY CONTROLS

- Of the **10** firms that received sanctions for QC violations
  - **Two** firms' registrations were revoked
  - **Eight** firms agreed to required undertakings as a part of their settlements
    - An independent consultant was additionally required as a part of the undertakings for one firm (Marcum LLP)
    - One firm's undertakings are only applicable in the event the Board grants any future registration application, as its prior petition to withdraw its registration was granted concurrent with the settlement (PMB Helin Donovan)

# OTHER NOTABLE ENFORCEMENT AREAS

- Data inception to Dec. 31, 2019, unless otherwise indicated



# IMPROPER ALTERATION OF AUDIT DOCUMENTATION

- Staff Practice Alert No. 14, Improper Alteration of Audit Documentation
  - Improper alteration of audit documentation in connection with an inspection or investigation can result in disciplinary actions with severe consequences (violations of duty to cooperate)
  - Issues in relatively recent oversight activities have heightened concerns about this at a range of firms, including global network affiliates
  - Consequences of improper alteration, in many cases, are more severe than from the underlying perceived audit deficiency

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STAFF AUDIT PRACTICE ALERT NO. 14

IMPROPER ALTERATION OF AUDIT  
DOCUMENTATION

APRIL 21, 2016

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Staff Audit Practice Alerts highlight new, emerging, or noteworthy circumstances that may affect how auditors conduct audits under, or otherwise comply with, the existing requirements of the standards and rules of the PCAOB and relevant laws. Auditors should determine the actions necessary to respond to these circumstances. The statements contained in Staff Audit Practice Alerts do not establish rules of the Board and do not reflect any Board determination or judgment about the conduct of any particular firm, auditor, or any other person.

The PCAOB staff has prepared this practice alert to emphasize that improperly altering audit documentation in connection with a PCAOB inspection or investigation violates PCAOB rules requiring cooperation with the Board's oversight activities and can result in disciplinary actions with severe consequences. Improperly altering audit documentation is also inconsistent with an auditor's professional duty to act with integrity and as a gatekeeper in the public securities markets. Evidence identified in connection with certain recent oversight activities has heightened the staff's concern about such misconduct.

Auditors should have a clear understanding of the requirements related to revising or supplementing documentation in compliance with PCAOB standards, which are described below. They should also understand that PCAOB staff is attentive to, and follows up on, indications of possible departures from those requirements, particularly in circumstances suggesting that auditors may have altered audit documentation in attempting to avoid detection of audit deficiencies by PCAOB inspections or enforcement staff. The consequences of providing improperly altered audit documentation to PCAOB inspectors or investigators may in many cases be far more severe than would be the consequences of the PCAOB staff identifying the audit deficiency that the revisions to the documentation attempt to obscure.

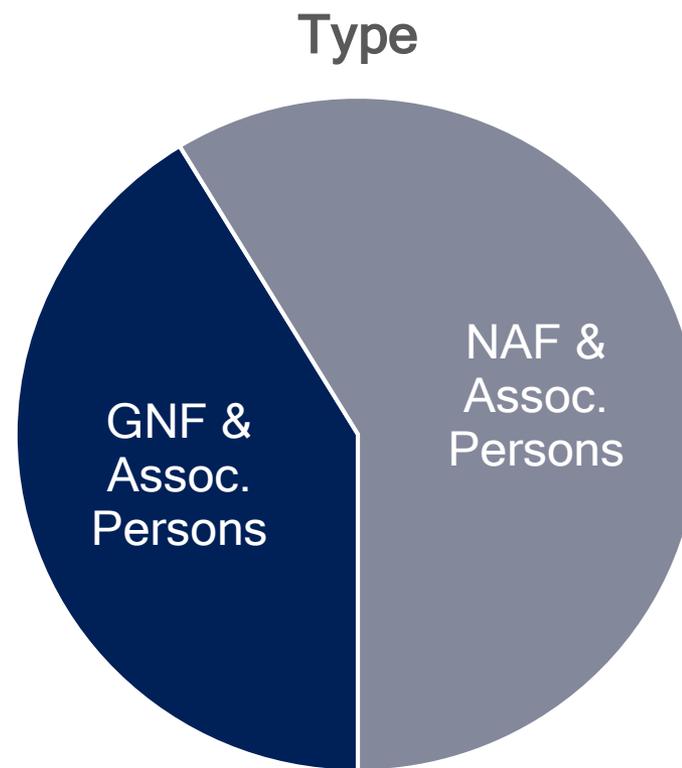
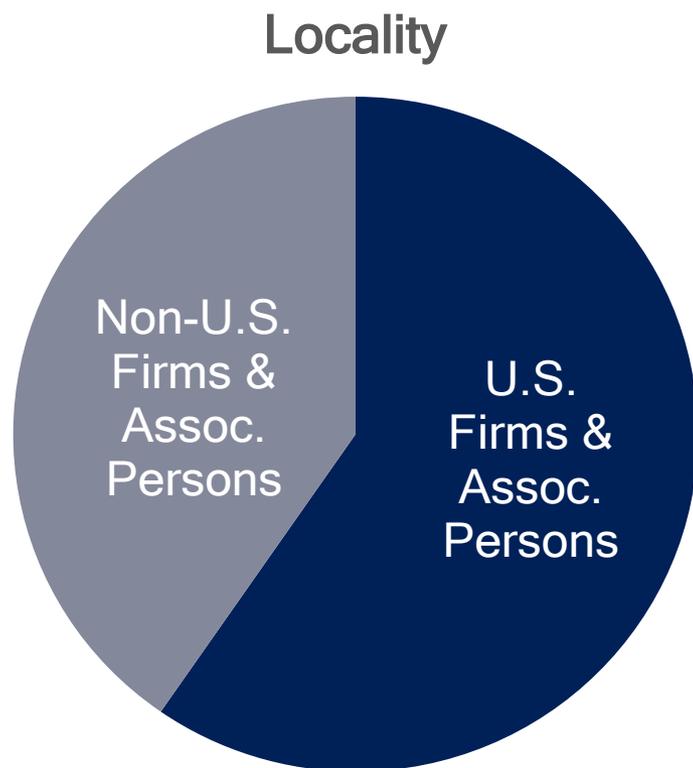
# INTERFERENCE IN BOARD PROCESSES

- Notwithstanding this practice alert, the Board continues to see violations of PCAOB Rules 4006 and 5110, which govern registered firms and associated person's conduct with respect to a Board inspection or investigation
  - **ZERO** tolerance for failing to provide information or interference with these processes
- These matters primarily involve providing improperly altered audit documentation to the Board in its inspections, or enforcement, processes
- These matters can be pursued in isolation, or in conjunction with other audit standards violations
- The Board has settled or finalized adjudication in more than **70** non-cooperation matters, involving more than **100** firms and associated persons



# INTERFERENCE IN BOARD PROCESSES

- Overall, about two-fifths of the respondents received a five year or permanent bar or revocation
- Overall, about one-third also involved other violations of auditing standards in the associated audits



Data through Dec. 31, 2019

# *IN THE MATTER OF CASTILLO MIRANDA Y COMPAÑÍA, S.C., ET AL. – OCT. 31, 2019*

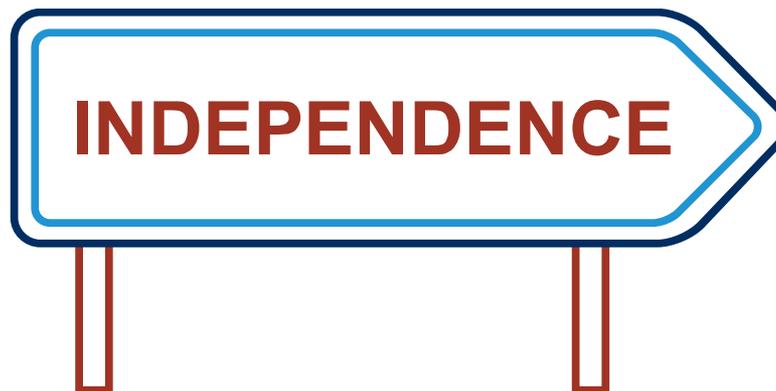
- Subsequent to the **BDO Mexico**'s notification of an upcoming inspection of two issuer audits, various partners and personnel of the firm improperly altered the audit documentation
  - Neither of the two sets of audit documentation were properly archived at the documentation completion date
- The firm made this improperly altered documentation available to inspectors
- The firm also had failed to implement policies and procedures to provide reasonable assurance its personnel would comply with audit documentation standards, and then failed to take corrective action after learning of the engagement personnel's violations

# *IN THE MATTER OF CASTILLO MIRANDA Y COMPAÑÍA, S.C., ET AL. – OCT. 31, 2019*

- The **firm and six associated persons** were censured
- The **six associated persons** also received combinations of bars (one to three year minimums) or suspensions, and civil monetary penalties
- A \$500,000 civil monetary penalty was imposed on the **BDO Mexico**, along with undertakings for certain remedial actions

# INDEPENDENCE MATTERS

- A registered public accounting firm and its associated persons must be independent of the firm's audit client throughout the audit and professional engagement period
  - To be recognized independent, an auditor must be free from any obligation to or interest in the audit client, its management or its owners
- The Board has found independence violations in several areas—one historically significant area is violations associated with maintaining the financial records or preparing financial statements for issuers and broker/dealers



# INDEPENDENCE MATTERS

- Since December 2014, the Board has entered into settled orders with certain associated persons for violations associated with maintaining the financial records or preparing financial statements of:
  - Broker-dealer audit clients – more than 25 orders
  - Issuer audit clients – about 10 orders
- Sanctions included:
  - Firms: censures, civil monetary penalties of \$2,500 – \$20,000, remedial measures, one year prohibitions on new clients
  - Associated Persons: censures, civil monetary penalties of \$2,500 – \$15,000, bars with a right to reapply of typically one or two years
- *In 2019, there were **no** settled matters involving independence failures due to preparation of financial statements*

# OTHER RECENT INDEPENDENCE MATTERS

- *In the Matter of Marcum LLP and A.G. Giugliano* – Sept. 10, 2019
  - The firm was sanctioned for
    - Impairing its independence with respect to **62 issuer audit clients** over four years by publicly advocating those clients as high-quality investment opportunities at firm hosted investor conferences
      - This created a mutual interest between the firm and its clients in whether their subsequent performance lived up to their touting
    - Failing to comply with quality control standards to provide reasonable assurance it would maintain independence in all required circumstances
  - Giugliano, the firm's head of independence, was sanctioned for substantially contributing to these violations by approving the conferences without considering the independence implications of touting its audit clients presenting at the conferences

# OTHER RECENT INDEPENDENCE MATTERS

- *In the Matter of Marcum LLP and A.G. Giugliano* – Sept. 10, 2019
  - **Marcum** was censured, received a civil monetary penalty of \$450,000 and was required to engage an independent consultant to review and make recommendations concerning the firm's policies, procedures, staffing and training with respect to auditor independence
  - **Giugliano** was censured and received a civil monetary penalty of \$25,000
- A parallel settlement, *In the Matter of Marcum Bernstein and Pinchuk LLP* – Sept. 10, 2019, was also approved with respect to similar independence violations by **Marcum LLP's affiliated firm**, which resulted in a censure of that firm, a civil monetary penalty of \$50,000 and requirement that the firm review and revise its policies and procedures with respect to auditor independence

# ENGAGEMENT QUALITY REVIEW MATTERS

- Engagement quality reviews are required for issuer audits and interim reviews, broker-dealer audits, and examinations/reviews of broker-dealer compliance/exemption reports
- The Board settled disciplinary orders in 2019 against **13** firms and associated persons for conduct relating to violations of EQR requirements
  - EQR violations were present where other audit standard or regulation violations were also present, in some cases
- **Two** of these matters settled in 2019 involved the EQR failing to maintain objectivity in performing the review

# SELECTED 2019 SETTLED MATTERS INVOLVING AUDIT STANDARDS VIOLATIONS

- *In the Matter of Jeffrey T. Gross Ltd. And Jeffrey T. Gross, CPA – July 23, 2019*
- *In the Matter of Timothy M. Kosiek – April 26, 2019*

# ***IN THE MATTER OF JEFFREY T. GROSS LTD. AND JEFFREY T. GROSS, CPA***

- **Gross and his firm** were sanctioned for multiple violations, including failing:
  - to obtain sufficient appropriate audit evidence in two audits
    - In one audit, he failed to establish and audit strategy and plan
    - In the other audit, he only obtained a year-end bank reconciliation and completed audit programs and checklists
  - to obtain engagement quality reviews for either audit
  - to timely file Forms AP in connection with the two audits, even after such had been brought to their attention by PCAOB inspectors
- Both audits were of issuers whose headquarters were in Eastern Europe, while he and his firm were based in Illinois
- **Gross** was barred and his **firm's** registration was revoked, both permanently

# ***IN THE MATTER OF TIMOTHY M. KOSIEK***

- **Kosiek**, a partner at Baker Tilly, was the engagement partner for the 2013 audit of Flagstar Bancorp, the holding company of Flagstar Bank, the largest bank in Michigan
- Kosiek failed to exercise due professional care and skepticism and failed to obtain sufficient appropriate audit evidence regarding the reported value and controls over Flagstar's allowance for loan and lease losses (ALLL)
  - Kosiek knew the ALLL was a high risk account and that the bank was under a consent order from its regulator, which had been critical of its method to estimate this allowance
    - In part to address its regulator's concerns, the bank changed its methodology for the ALLL in 2013

# IN THE MATTER OF TIMOTHY M. KOSIEK

- Kosiek concurred with the new ALLL methodology, which excluded loss history of non-performing loans, but didn't notice audit documentation indicating that the planned qualitative adjustment for non-performing loans had not been applied
  - Kosiek was also aware that under the new methodology, Flagstar's ALLL for 2013 was reduced by about one-third and the corresponding expense against earnings reduced significantly more
- He also didn't adequately evaluate the design of Flagstar's ALLL controls over valuation and learned that existing controls were not operating effectively
- Furthermore, Kosiek failed to perform substantive procedures on loan files and to perform a retrospective review of the ALLL
- **Kosiek** was censured, barred with the right to reapply after two years, and a paid a civil monetary penalty of \$25,000

# EXTRAORDINARY COOPERATION CREDIT

- Extraordinary cooperation is voluntary and timely action, beyond compliance with legal or regulatory obligations, that contributes to the mission of the Board
- Three types:
  - self-reporting
  - remedial or corrective action
  - substantial assistance to the Board's investigative processes or to other law enforcement authorities



[Policy Statement regarding Credit for Extraordinary Cooperation in Connection with Board Investigations](#)



# EXTRAORDINARY COOPERATION CREDIT

- The Board previously disclosed that **two** unnamed broker-dealer audit firms had prepared financial statements, but would not be sanctioned based on the firms' receiving credit for extraordinary cooperation for:
  - Timely and voluntary self-reporting to the PCAOB Tip Line
  - Timely, voluntary, and meaningful remedial actions, including, in one matter, communicating the violation to the client and discussing the conduct and violation at an annual firm training
- On October 31, 2019, sanctions credit was given *In the Matter of Deloitte Anjin LLC* as the firm provided substantial assistance by:
  - Voluntarily and timely self-reporting the misconduct
  - Providing substantial assistance to the PCAOB's investigation, including sharing the results of its own internal investigation
  - Separating certain personnel it identified as responsible
  - Implementing relevant quality control system enhancements

# TERMINATIONS OF BARS

- PCAOB Rule 5302(b) governs petitions to terminate a bar
  - Specific items outlined in the PCAOB Rules 5302(b)(2), 5302(b)(3), and 5302(b)(4) must be addressed for the Board to consider a petitioner's request
- Through June 30, 2020, **13 individuals** have successfully terminated their bars
  - One each in 2009, 2010, 2016 and 2017
  - Three in 2018
  - One in 2019
  - Five in 2020 (through June 30)

# PCAOB CENTER FOR ENFORCEMENT TIPS, COMPLAINTS AND OTHER INFORMATION

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# QUESTIONS

Please submit any questions or feedback you might have on this presentation to [forum@pcaobus.org](mailto:forum@pcaobus.org).

