



1666 K Street, N.W.  
Washington, DC 20006  
Telephone: (202) 207-9100  
Facsimile: (202) 862-8430  
[www.pcaobus.org](http://www.pcaobus.org)

## **Inspection of Edwards Sauer & Owens**

**Issued by the  
Public Company Accounting Oversight Board  
July 13, 2006**

**THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT**

**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. 104-2006-143



### **Notes Concerning this Report**

1. Portions of this report may describe deficiencies or potential deficiencies in the systems, policies, procedures, practices, or conduct of the firm that is the subject of this report. The express inclusion of certain deficiencies and potential deficiencies, however, should not be construed to support any negative inference that any other aspect of the firm's systems, policies, procedures, practices, or conduct is approved or condoned by the Board or judged by the Board to comply with laws, rules, and professional standards.
2. Any references in this report to violations or potential violations of law, rules, or professional standards should be understood in the supervisory context in which this report was prepared. Any such references are not a result of an adversarial adjudicative process and do not constitute conclusive findings of fact or of violations for purposes of imposing legal liability. Similarly, any description herein of a firm's cooperation in addressing issues constructively should not be construed, and is not construed by the Board, as an admission, for purposes of potential legal liability, of any violation.
3. Board inspections encompass, among other things, whether the firm has failed to identify departures from Generally Accepted Accounting Principles ("GAAP") in its audits of financial statements. This report's descriptions of any such auditing failures necessarily involve descriptions of the related GAAP departures. The Board, however, has no authority to prescribe the form or content of an issuer's financial statements. That authority, and the authority to make binding determinations concerning an issuer's compliance with GAAP, rests with the Securities and Exchange Commission ("SEC" or "Commission"). Any description, in this report, of perceived departures from GAAP should not be understood as an indication that the Commission has considered or made any determination regarding these GAAP issues unless otherwise expressly stated.



## INSPECTION OF EDWARDS SAUER & OWENS

The Public Company Accounting Oversight Board ("PCAOB" or "the Board") has conducted an inspection of the registered public accounting firm Edwards Sauer & Owens ("the Firm"). The Board is issuing this report of that inspection in accordance with the requirements of the Sarbanes-Oxley Act of 2002 ("the Act").

The Board is making portions of the report publicly available. Specifically, the Board is releasing to the public Part I of the report and portions of Part IV of the report. Part IV of the report consists of the Firm's comments, if any, on a draft of the report.<sup>1/</sup>

The Board has elsewhere described in detail its approach to making inspection-related information publicly available consistent with legal restrictions.<sup>2/</sup> A substantial portion of the Board's criticisms of a firm (specifically criticisms of the firm's quality control system), and the Board's dialogue with the firm about those criticisms, occurs out of public view, unless the firm fails to make progress to the Board's satisfaction in addressing those criticisms. In addition, the Board generally does not disclose otherwise nonpublic information, learned through inspections, about the firm or its clients. Accordingly, information in those categories generally does not appear in the publicly available portion of an inspection report.

---

<sup>1/</sup> The Board does not make public any of a firm's comments that address a nonpublic portion of the report. In addition, pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(b), if a firm requests, and the Board grants, confidential treatment for any of the firm's comments on a draft report, the Board does not include those comments in the final report at all. The Board notes that it routinely grants confidential treatment, if requested, for any of a firm's comments that identify factually inaccurate statements in the draft that the Board corrects in the final report.

<sup>2/</sup> See Statement Concerning the Issuance of Inspection Reports, PCAOB Release No. 104-2004-001 (August 26, 2004).

**PART I**

**INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS**

Members of the Board's inspection staff ("the inspection team") conducted fieldwork for the inspection from May 9, 2005 to May 12, 2005. The fieldwork included procedures tailored to the nature of the Firm, certain aspects of which the inspection team understood at the outset of the inspection to be as follows:

Number of offices	2 (Pittsburgh and Altoona, Pennsylvania)
Ownership structure	Professional corporation
Number of partners	5
Number of professional staff <sup>3/</sup>	10
Number of issuer audit clients <sup>4/</sup>	2

Board inspections are designed to identify and address weaknesses and deficiencies related to how a firm conducts audits. To achieve that goal, Board inspections include reviews of certain aspects of selected audits performed by the firm and reviews of other matters related to the firm's quality control system.

In the course of reviewing aspects of selected audits, an inspection may identify ways in which a particular audit is deficient, including failures by the firm to identify, or to

---

<sup>3/</sup> "Professional staff" includes all personnel of the Firm, except partners or shareholders and administrative support personnel. The number of partners and professional staff is provided here as an indication of the size of the Firm, and does not necessarily represent the number of the Firm's professionals who participate in audits of issuers or are "associated persons" (as defined in the Act) of the Firm.

<sup>4/</sup> The number of issuer audit clients shown here is based on the Firm's self-reporting and the inspection team's review of certain information for inspection planning purposes. It does not reflect any Board determination concerning which, or how many, of the Firm's audit clients are "issuers" as defined in the Act.

address appropriately, respects in which an issuer's financial statements do not present fairly the financial position, results of operations, or cash flows of the issuer in conformity with GAAP.<sup>5/</sup> It is not the purpose of an inspection, however, to review all of a firm's audits or to identify every respect in which a reviewed audit is deficient. Accordingly, a Board inspection report should not be understood to provide any assurance that the firm's audits, or its issuer clients' financial statements, are free of any deficiencies not specifically described in an inspection report.

A. Review of Audit Engagements

The scope of the inspection procedures performed included reviews of aspects of the performance of both of the Firm's audits of the financial statements of issuers. Those aspects were selected according to the Board's criteria, and the Firm was not allowed an opportunity to limit or influence the selection process.

The inspection team identified matters that it considered to be audit deficiencies.<sup>6/</sup> The deficiencies identified in both of the audits reviewed included deficiencies of such significance that it appeared to the inspection team that the Firm did not obtain sufficient competent evidential matter to support its opinion on the issuer's financial statements. Those deficiencies included –

- (1) the failure to perform and document adequate audit procedures related to the issuer's allowance for loan losses; and

---

<sup>5/</sup> When it comes to the Board's attention that an issuer's financial statements appear not to present fairly, in a material respect, the financial position, results of operations or cash flows of the issuer in conformity with GAAP, the Board reports that information to the SEC, which has jurisdiction to determine proper accounting in issuers' financial statements.

<sup>6/</sup> PCAOB standards require a firm to take appropriate actions to assess the importance of audit deficiencies identified after the date of the audit report to the firm's present ability to support its previously expressed opinions. See AU 390, *Consideration of Omitted Procedures After the Report Date*, and AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report* (both included among the PCAOB's interim auditing standards, pursuant to PCAOB Rule 3200T). Failure to comply with these PCAOB standards could be a basis for Board disciplinary sanctions.

(2) on two engagements, the failure to perform and document appropriate procedures to support the Firm's reliance on controls at significant third-party service organizations.

**B. Review of Quality Control System**

In addition to evaluating the quality of the audit work performed on specific audits, the inspection included review of certain of the Firm's practices, policies and procedures related to audit quality. This review addressed practices, policies and procedures concerning audit performance, training, compliance with independence standards, client acceptance and retention, and the establishment of policies and procedures. As described above, any defects in, or criticisms of, the Firm's quality control system are discussed in the nonpublic portion of this report and will remain nonpublic unless the Firm fails to address them to the Board's satisfaction within 12 months of the date of this report.

END OF PART I



PCAOB Release No. 104-2006-143  
Inspection of Edwards Sauer & Owens  
July 13, 2006  
Page 5

PARTS II AND III OF THIS REPORT ARE NONPUBLIC  
AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

## **PART IV**

### **RESPONSE OF THE FIRM TO 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 provided a written response.

Pursuant to section 104(f) of the Act and PCAOB Rule 4007(b), if a firm requests, and the Board grants, confidential treatment for any of the firm's comments on a draft report, the Board does not include those comments in the final report. The Board routinely grants confidential treatment, if requested, for any of a firm's comments that identify factually inaccurate statements in the draft that the Board corrects in the final report.

Pursuant to section 104(f) of the Act and PCAOB Rule 4007(b), the Firm's response, minus any portion granted confidential treatment, is attached hereto and made part of this final inspection report. In any version of this report that the Board makes publicly available, any portions of the Firm's response that address nonpublic portions of the report are omitted.

**EDWARDS  
SAUER &  
OWENS, P.C.**

**Certified Public Accountants & Business Advisors**

500 Warner Centre, 332 Fifth Avenue, Pittsburgh, PA 15222  
Phone: 412-281-9211 Fax: 412-281-2407  
www.esocpa.com  
April 13, 2006

A Professional Corporation  
Direct Dial:

Mr. George Diacont, Director  
Division of Registration and Inspections  
Public Company Accounting Oversight Board  
1666 K Street, N.W.  
Washington, DC 20006

**Re: Edwards Sauer & Owens, P.C.  
Response to Part I of the Draft Report of Inspection**

Dear Mr. Diacont:

We appreciate the opportunity to respond to the Public Company Accounting Oversight Board's draft report, dated March 16, 2006, regarding the 2005 inspection of Edwards Sauer & Owens, P.C.

We respectfully disagree with the inspector's statement that our firm did not obtain sufficient competent evidential matter to support our opinion as related to the allowance for loan losses. We believe that the documentation included in the audit workpapers, our quarterly reviews of the financial statements, our knowledge of the issuer, discussions with management, the issuer's history of net charge-offs, and review of regulatory exams of the issuer support our opinion regarding the allowance for loan losses as of December 31, 2004. We understand that the allowance for loan losses represents an estimate requiring a high degree of judgment both by the issuer and the external auditor. Accounting literature also requires the issuer to develop and utilize a consistent and reasonable methodology to support their estimate, which we believe is present with this issuer. Based upon all of the factors, we believe that we have supported our opinion regarding the allowance for loan losses. After discussions with the inspector, we performed additional procedures based upon the inspector's comments and no new facts came to our attention that would change our previously issued opinion.

With regard to the comment concerning performance and documentation related to the reliance on controls at a significant third-party service organization, we respectfully disagree. We obtained and reviewed the service organization's SAS #70 report as of September 30, 2004, noting no material weaknesses. We inquired of management and documented their responses related to internal controls as they pertain to the third party servicer and we performed our entire substantive testing after September 30, 2004 to obtain competent evidential matter regarding the financial statement taken as a whole. In addition, we performed various other audit procedures and testing which lead us to believe that the procedures we performed throughout the audits supplies us with competent evidential matter to support our opinions. After discussions with the inspector, we obtained additional evidence to support that there were no changes in controls from September 30, 2004 to December 31, 2004 at the service organization or the issuers.

We support the inspection process and are committed to working with the PCAOB staff. We also appreciate the opportunity to respond to these comments and would be pleased to discuss our responses with the PCAOB.

Respectfully submitted,

*Edwards Sauer & Owens, P.C.*

Edwards Sauer & Owens, P.C.