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**Inspection of  
Harold J. Nicholson, Chartered**

**Issued by the  
Public Company Accounting Oversight Board  
January 25, 2007**

**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. 104-2007-006**



### **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 U.S. Generally Accepted Accounting Principles ("GAAP") or Securities and Exchange Commission ("SEC" or "Commission") disclosure requirements in its audits of financial statements. This report's descriptions of any such auditing failures necessarily involve descriptions of the related GAAP or disclosure 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 or Commission disclosure requirements, rests with the Commission. Any description, in this report, of perceived departures from GAAP or Commission disclosure requirements should not be understood as an indication that the Commission has considered or made any determination regarding these issues unless otherwise expressly stated.



## INSPECTION OF HAROLD J. NICHOLSON, CHARTERED

The Public Company Accounting Oversight Board ("PCAOB" or "the Board") has conducted an inspection of the registered public accounting firm Harold J. Nicholson, Chartered ("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.

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<sup>1/</sup> The Board does not make public any of a firm's comments that address a nonpublic portion of the report unless a firm specifically requests otherwise. 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 routinely grants confidential treatment, if requested, for any portion of a firm's response that addresses any point in the draft that the Board omits form, or any inaccurate statement 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 1, 2006 to May 5, 2006. 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	1 (Overland Park, Kansas)
Ownership structure	Professional corporation
Number of partners	1
Number of professional staff <sup>3/</sup>	1
Number of issuer audit clients <sup>4/</sup>	1

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.

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<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. In some circumstances, a Board inspection may include a review of a firm's audit of financial statements of an issuer that ceased to be an audit client before the inspection, and any such former clients are not included in the number shown here.

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 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 Engagement

The inspection procedures included a review of aspects of the Firm's auditing of financial statements of one issuer. The scope of this review was determined according to the Board's criteria, and the Firm was not allowed an opportunity to limit or influence the scope.

The inspection team identified what it considered to be an audit deficiency<sup>6/</sup> 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 relevant financial

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<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's practice is to report 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.

statements.<sup>7/</sup> That deficiency was the failure to perform sufficient audit procedures to test the existence of revenue-producing assets leased to customers.

B. Review of Quality Control System

In addition to evaluating the quality of the audit work performed on a specific audit, 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

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<sup>7/</sup> In some cases, an inspection team's observation that a firm failed to perform a procedure may be based on the absence of documentation and the absence of persuasive other evidence, even if a firm claims to have performed the procedure. PCAOB Auditing Standard No. 3, *Audit Documentation*, ("AS No. 3") provides that, in various circumstances including PCAOB inspections, a firm that has not adequately documented that it performed a procedure, obtained evidence, or reached an appropriate conclusion must demonstrate with persuasive other evidence that it did so, and that oral assertions and explanations alone do not constitute persuasive other evidence. See AS No. 3, paragraph 9; Appendix A to AS No. 3, paragraph A28. For purposes of the inspection, an observation that the Firm did not perform a procedure, obtain evidence, or reach an appropriate conclusion may be based on the absence of such documentation and the absence of persuasive other evidence.



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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 Firm provided a written response to a draft of this 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.<sup>8/</sup>

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<sup>8/</sup> 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 unless a firm specifically requests otherwise. In some cases, the result may be that none of a firm's response is made publicly available.

**HAROLD J. NICHOLSON, CHARTERED**  
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913-236-4435

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November 27, 2006

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

Re: Response to Part I of the Draft Report of Inspection of Harold J. Nicholson, Chartered

Dear Mr. Diacont:

We want to thank you for the opportunity to review the draft report of the inspection of Harold J. Nicholson, Chartered dated October 26, 2006, and appreciate the opportunity to respond to the findings in that report. While we strive to provide excellent service to our clients, we recognize that a different perspective can improve the quality of our audits.

The following comments are in response to *Part I - Inspection Procedures and Certain Observations* in the report. The inspection team identified one audit deficiency which indicated that the firm did not obtain sufficient competent evidential matter to support the opinion on the issuer's financial statements. Specifically, the inspection team did not think that the firm performed sufficient audit procedures to test the existence of revenue-producing assets leased to customers.

We believe that sufficient audit procedures were performed by the firm to support its opinion on the issuer's financial statements. Part .22 of AU Section 326, *Evidential Matter*, states "The independent auditor's objective is to obtain sufficient competent evidential matter to provide him or her with a reasonable basis for forming an opinion." In addition, AU Section 326.23, "...the auditor's opinion, to be economically useful, must be formed within a reasonable length of time and at reasonable cost."

The assets in question are hundreds of trailers and containers which are leased to customers who are located throughout the country. Although one customer may lease a significant number of the leased assets, the assets are not normally in one location. In our judgment, it was not practical from a time or economic standpoint to physically observe a significant number of the leased assets in the possession of the customers. We did observe 100% of the trailers and containers that were at the client's facility on a date of our choosing and did not encounter any exceptions.

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Letter to Mr. George H. Diacont  
November 27, 2006

AU Section 390, *Consideration of Omitted Procedures After the Report Date*, part .04 states "...the results of other procedures that were applied may tend to compensate for the one omitted or make its omission less important." While we do not think a procedure was omitted by us, we refer to this since we feel that a procedure was omitted in the judgment of the inspection team. During the 2004 audit, we telephoned a representative test group of customers to determine if they indeed had the assets that the issuer's records indicated were being leased. We did not encounter any exceptions to this procedure.

We did not perform this procedure for the 2005 audit, however, the leased asset identification numbers were cross checked to the accounts receivable invoices for those customers who were circularized. We do agree that our audit documentation should be improved. Since we confirmed a significant dollar amount of accounts receivable balances, we felt that this also indirectly confirmed the existence of the leased assets. In our judgement, the customers would not acknowledge the correctness of a balance owed if the revenue-producing asset was not in their possession as of the date of the confirmation.

While we feel that we did obtain overall sufficient audit support for the existence of the revenue-producing assets leased to customers, we acknowledge that our overall audit documentation in this area should, and will be, improved on future engagements. For the 2006 audit, we will send a listing of the leased assets with each of the accounts receivable confirmations that are circularized so that the existence of the leased assets are also specifically and directly confirmed by the customers. AU Section 390, part .04 referred to above further states "Also, subsequent audits may provide audit evidence in support of the previously expressed opinion."

Since a significant number of the accounts receivable balances for the 2006 audit will also be confirmed as of December 31, 2006, we do not feel that it is necessary at this time to perform additional procedures for 2005 unless it is determined that the audit findings in the 2006 audit indicate that a problem exists that would also affect the prior year.

Again, we support the mission of the PCAOB and the inspection process. We want to work with them to achieve our common goals. Please contact Harold J. Nicholson at (913) 236-4435 with any questions.

Sincerely,



Harold J. Nicholson, Chartered