



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

**Inspection of
Virchow, Krause & Company, LLP**

**Issued by the
Public Company Accounting Oversight Board**

June 14, 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. 104-2007-085



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 VIRCHOW, KRAUSE & COMPANY, LLP

The Public Company Accounting Oversight Board ("PCAOB" or "the Board") has conducted an inspection of the registered public accounting firm Virchow, Krause & Company, LLP ("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.^{1/}

The Board has elsewhere described in detail its approach to making inspection-related information publicly available consistent with legal restrictions.^{2/} 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.

^{1/} 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 from, or any inaccurate statement in the draft that the Board corrects in, the final report.

^{2/} 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 June 26, 2006 to June 28, 2006 and from July 10, 2006 to July 14, 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	14 (Appleton, Eau Claire, Elkhorn, Green Bay, Janesville, Madison, Milwaukee, Oshkosh and Wausau, Wisconsin; Chicago and Oakbrook, Illinois; Detroit and Southfield, Michigan; Minneapolis, Minnesota)
Ownership structure	Limited liability partnership
Number of partners	147
Number of professional staff ^{3/}	883
Number of issuer audit clients ^{4/}	43

^{3/} "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.

^{4/} 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.

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 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.^{5/} 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 inspection procedures included a review of aspects of the Firm's auditing of financial statements of nine issuers. 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 audit deficiencies.^{6/} The deficiencies identified in three of the audits reviewed included deficiencies of such

^{5/} 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.

^{6/} 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.

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.^{7/} Those deficiencies were –

- (1) the failure to perform sufficient procedures with respect to revenue recognition;
- (2) the failure to perform sufficient procedures to evaluate potential impairment of intangible assets; and
- (3) the inappropriate reliance on controls over inventory valuation.

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

^{7/} 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.



PCAOB Release No. 104-2007-085
Inspection of Virchow, Krause &
Company, LLP
June 14, 2007
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 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.^{8/}

^{8/} 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.



March 12, 2007

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

RE: Virchow, Krause & Company, LLP Response to the Public Company Oversight Board Draft on the 2006 Inspection

Dear Mr. Diacont:

Virchow, Krause & Company, LLP (the "Firm") appreciates the opportunity to respond to the Public Company Accounting Oversight Board (the "PCAOB") Draft Report on the 2006 Inspection of Virchow Krause & Company, LLP.

The Firm is committed to the highest standards of audit quality. We have thoroughly considered the Board's comments addressed in the Draft Report, and have assessed whether we have already initiated actions on a firm wide basis that address those comments. After addressing each of the specific comments raised in the report, we are determining the extent to which further actions are necessary.

As part of our commitment to high quality, we have been implementing enhancements to our audit methodology and delivery, including an extensive investment in training, improving our audit technology, significantly improving our own internal review process and, where necessary, hiring additional resources.

We appreciate the constructive dialogue we have had with the PCAOB Inspection Staff in connection with the inspection process. Further, we support the Board's effort to improve the quality of the public reporting process.

We would be pleased to discuss any aspect of our response or to address any other questions you may have.

We have the following additional comments regarding the matters described in the Report.

Issuer A – We respectfully disagree with this comment. All the information necessary to reach the conclusion we reached with regard to the contract in question was available in our work papers, or in specific reports referred to in our work papers. Based on the comments the PCAOB made, we evidently did not accumulate and present the information concerning this contract in a form that could be easily understood by an inspector. In the future, we will continue to improve our work paper documentation in an effort to make it easier for an experienced audit inspector to follow our audit trail. However, we audited all the numbers related to the contract and are confident that our work papers were of sufficient quality to support our opinion on the issuer's financial statements.

Mr. George H. Diacont, Director
Division of Registration and Inspections
Public Company Oversight Board

March 12, 2007
Page 2

Issuer B – We respectfully disagree with this comment. Even if there was a 100% guarantee that the intangible asset would have been fully realized, our opinion would not have been affected. Issuer B would still have received a going concern opinion, as they had in the previous year. Had we rendered a clean opinion on Issuer B's financial statements when it was inappropriate to do so, then the comment would seem more appropriate. To put this into proper perspective, Issuer B's largest asset at the time was \$379,291 of prepaid expenses, which accounted for 41% of total assets. Total assets were one seventh (1/7) of the net loss for the year, and one forty-fourth (1/44) of the accumulated deficit. On the other hand, if the intangible assets had been completely written-off, we still would have issued a going concern opinion, as occurred in 2006. Either way, no matter what that asset's value was, it did not affect our opinion in any year we reported on. We believe our opinion was appropriate.

Issuer C – We respectfully disagree with this comment. The context of this issue needs to be explained in order to put the comment into perspective. We selected 42 items to determine whether we could achieve a level of comfort with regard to the client's inventory pricing mechanism. It should be noted that achieving a level of comfort with regard to the performance of their pricing mechanism should not be confused with testing the client's system of internal control. That is, we did not conduct any tests to determine whether, as a part of the client's pricing process, any controls were in place and operating effectively. We were testing the effectiveness of the design of the system and the resulting valuation, not any controls that might have ensured its accuracy. Consequently, the comment that we placed unwarranted reliance on a system of internal control that we did not identify as such, or test, seems unwarranted.

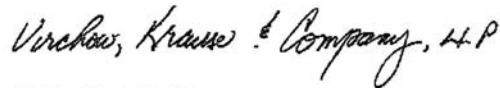
* * * * *

We appreciate the opportunity to provide our response to the Report and look forward to continuing to work with the PCAOB on matters of interest to our public company auditing practice.

Please contact R. Bruce Cole at 608.240.2312 with any questions.

Sincerely,

VIRCHOW, KRAUSE & COMPANY, LLP



c: Mr. Timothy L. Christen
Mr. Brandon D. Andries
Mr. Scott G. Ebert
Mr. Kim L. Tredinnick
Ms. Carla A. Gogin