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## **Inspection of Mason Russell West, LLC**

**Issued by the**

**Public Company Accounting Oversight Board**

**April 6, 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. 104-2006-094A  
(Includes portions of Parts II and IV of the full report that  
were not included in PCAOB Release No. 104-2006-094)



### **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 MASON RUSSELL WEST, LLC

The Public Company Accounting Oversight Board ("PCAOB" or "the Board") has conducted an inspection of the registered public accounting firm Mason Russell West, LLC ("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. 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 17, 2005 to May 19, 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	1 (Littleton, Colorado)
Ownership structure	Limited liability company
Number of partners	2
Number of professional staff <sup>3/</sup>	2
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 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

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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.

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 engagement reviews did not identify any audit performance issues that, in the inspection team's view, resulted in the Firm failing to obtain sufficient competent evidential matter to support its opinion on the issuer's financial statements.

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

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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 reports that information to the SEC, which has jurisdiction to determine proper accounting in issuers' financial statements.



PCAOB Release No. 104-2006-094A  
Inspection of Mason Russell West, LLC  
April 6, 2006  
Page 4

PORTIONS OF THE REST OF THIS REPORT ARE NONPUBLIC AND ARE OMITTED  
FROM THIS PUBLIC DOCUMENT

## PART II

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### A. Issues Related to Quality Controls

The inspection of the Firm included consideration of aspects of the Firm's system of quality control. Assessment of a firm's quality control system rests both on review of a firm's stated quality control policies and procedures and on inferences that can be drawn from respects in which a firm's system has failed to assure quality in the actual performance of engagements.<sup>6/</sup> On the basis of the information reported by the inspection team, the Board has the following concerns about aspects of the Firm's system of quality control.

1. Audit Performance
  - a. Auditor Communications

The Firm's system of quality control does not provide sufficient assurance that the Firm will make or document all required auditor communications with audit committees, including making independence confirmations required by Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committees*, and formally documenting communications with audit committees. [Issuers A and B]

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<sup>6/</sup> A firm's failure to comply with the requirements of PCAOB standards when performing an audit may be an indication of a potentially significant defect in a firm's quality control system even if that failure did not result in an insufficiently supported audit opinion.

## **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.

## Mason Russell West, LLC

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E-MAIL: cpas@mrwllc.com

DICK MASON  
RAY RUSSELL, JR.

CERTIFIED PUBLIC ACCOUNTANTS  
CONSULTING SERVICES

February 3, 2006

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

Dear Mr. Diacont:

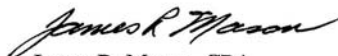
Attached are our responses to Part I and Part II of the Report of Inspections. We have separated our response to Part I to ensure the response is easily accessible to allow you to include it in the publicly available report. Our responses to Part II include any changes to our quality control system or any changes to procedures and or programs to help strengthen our audit quality.

It should be noted here that we strongly disagree with the inspection teams findings that we did not perform adequate auditing procedures related to the inventory of Issuer A. Our reasons are included in our response to both Part I and Part II.

It isn't that we think our audits can't be improved, they can and should. We do think it was a leap from should have done more to "insufficiently supported audit report".

You will receive a copy of this report by fax and the original by Fed Ex.

Sincerely,



James R. Mason, CPA  
Mason Russell West, LLC



**Response to Part 1, Item A of the Detailed Discussion of the Inspection results.**

We strongly disagree with the contention that our audit procedures were insufficient to support our opinion on the financial statements.

The statement that there is no evidence in the audit file that we performed adequate audit procedures to test the existence and valuation of inventory is completely inaccurate.

The basis of the team's comments appears to be the use of the Stock Status Report and the >\$3,000 item listing. The statement made makes it appear that we just accepted those reports without further tests being performed. These reports were used only as guides during the inventory test count and were not the basis upon which we issued our opinion. We performed an inventory observation and other inventory audit steps that are included in the work papers and outlined as follows:

**Inventory Count Tag Verification**

Count tags were reconciled and tested for each area of inventory in the plant. Tags not used were accounted for. All areas were tested to make sure there were tags on each item within that area. Void tags were noted and accounted for. There were no shipments received or sent during the inventory, nor was there any movement between raw materials, work-in-process and finished goods during the inventory observation. All of these items are noted on the audit work papers.

**Inventory Observation Count**

There were approximately 130 items tested during the count. Approximately 50% of these were from perpetual inventory records to the floor and 50% were from the floor to the perpetual inventory records. While the count was in process, we used as a guide only, a listing of product in excess of \$3,000 (a high cost inventory listing). We chose specific items from this guide during our floor to perpetual and perpetual to floor testing to make sure we covered a sample of the higher cost items. In addition, we tested other items off this guide to verify counts on this listing.

**Comparison of Count to Stock Status Report**

Items test counted in the physical inventory were traced to the stock status report to verify that the amounts listed on the final computer generated perpetual inventory report agreed to the counts arrived at during the physical inventory. This test ensured that the stock status report was correct and had valid quantities. This test was performed for both items tested by us during the physical inventory and items not tested. The stock status report was also agreed to the general ledger and financial statements.

**Price Testing**

Prices were tested and extensions of price and quantity were proofed. Some of the price tests were verifications that last years price had not changed and there were no purchases during the current year of those items. All other price tests for raw materials were traced to current invoices, vendor price lists, etc. Any exceptions noted were discussed with

client personnel and corrected prior to printing the final stock status report, the final page of which is in our audit work papers.

**Comparison of Gross Profit Percentage, Cost of Sales, and Other Factors**

We also performed analytical procedures that compared cost of sales percentages and gross profit percentages with the firm's past history and noted no significant variations in these ratios. Inventory turnover remained stable.

Our experience with this client has shown that the count teams are conscientious and all personnel involved with the physical inventory are striving for a no exception inventory count.

We are not required to test through the system if sufficient competent evidential matter available to test the system output. Our auditor's judgment determined there was sufficient, competent evidential matter available and the above tests confirmed that judgment. The evidential matter tested supports our opinion on the existence and valuation of inventory and the financial statements.

REDACTED

Comments on Non-public Aspects of Report

We were in the process of developing a SAS 61 documentation form when the team was in our offices reviewing these engagements. We did verbally discuss the audit committee communications with these clients. We have since established a requirement that our documentation form must be in all files that have an audit committee and all SEC engagements regardless whether the communication is verbal or written.

REDACTED

Comments on Non-public Aspects of Report