

**Inspection of  
Michael F. Albanese CPA**

**Issued by the  
Public Company Accounting Oversight Board  
September 30, 2008**

**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**



### **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 MICHAEL F. ALBANESE CPA

The Public Company Accounting Oversight Board ("PCAOB" or "the Board") has conducted an inspection of the registered public accounting firm Michael F. Albanese CPA. 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 from, 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 29, 2007 to June 4, 2007. 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 (Parsippany, New Jersey) |
| Ownership structure                          | Sole practitioner          |
| Number of partners                           | 1                          |
| Number of professional staff <sup>3/</sup>   | None                       |
| 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.<sup>5/</sup> 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.

<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.

<sup>5/</sup> This focus necessarily carries through to reports on inspections and, accordingly, Board inspection reports are not intended to serve as balanced report cards or overall rating tools.

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>6/</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 audit deficiencies.<sup>7/</sup> The deficiencies identified in the audit reviewed included a deficiency 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.<sup>8/</sup> That

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<sup>6/</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>7/</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.

<sup>8/</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

deficiency was the failure to perform sufficient audit procedures to evaluate the appropriateness of the issuer's accounting related to the conversion of debt to common stock.

The deficiency described above related to auditing an aspect of an issuer's financial statements that the issuer revised in a restatement subsequent to inspection fieldwork.<sup>9/</sup>

#### 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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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.

<sup>9/</sup> The Board inspection process did not include review of any additional audit work related to the restatement.



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

## PART II

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### B. 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>10/</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.

#### Audit Performance

A firm's system of quality control should provide reasonable assurance that the work performed on an audit engagement will meet applicable professional standards and regulatory requirements. On the basis of the information reported by the inspection team, including the audit performance deficiency described in Part II.A and any other deficiencies identified below, the Board has concerns that the Firm's system of quality control fails to provide such reasonable assurance in at least the following respects<sup>11/</sup> –

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<sup>10/</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.

<sup>11/</sup> In addition to the points described in the text, the Board notes that the concurring partner review procedure used by the Firm for the issuer inspected did not result in the identification of the deficiency noted by the inspection team. Because the Firm was not a member of the SEC Practice Section of the American Institute of Certified Public Accountants and therefore is not subject to the concurring partner review requirement in the Board's interim standards, the Board is not here addressing the concurring partner review procedures in terms of a criticism of, or a potential defect in, the Firm's quality control systems for purposes of PCAOB Rule 4009 (discussed in Part III below). Nevertheless, the Board notes the important role that an effective concurring partner review can play in ensuring that an audit is performed in compliance

a. Technical Competence, Due Care, and Professional Skepticism

The Firm's system of quality control appears not to do enough to ensure technical competence and the exercise of due care or professional skepticism.

b. Engagement Completion Document

The Firm's system of quality control appears not to provide sufficient assurance that the Firm will prepare an engagement completion document in accordance with AS No. 3 which is necessary to demonstrate that the work performed by engagement personnel addresses the significant findings and issues of the engagement. [Issuer A]

c. Auditor Communications

The Firm's system of quality control appears not to provide sufficient assurance that the required auditor communications to the audit committee, or equivalent, occur and are appropriately documented. [Issuer A]

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with PCAOB standards, and encourages the Firm to obtain a meaningful concurring partner review by a qualified reviewer in connection with audits of issuers. A meaningful concurring partner review procedure would likely have identified the deficiencies described in this report before the Firm issued the reports.

**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>12/</sup>

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<sup>12/</sup> In any version of an inspection report that the Board makes publicly available, any portions of a firm's response that address nonpublic portions of the report are omitted. In some cases, the result may be that none of a firm's response is made publicly available.

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June 30, 2008

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 and II of the Draft Report on the 2008 Inspection of Michael F. Albanese, CPA**

I have received the draft of the above mentioned Report and appreciate the ability to respond. I welcome the inspection process that the Public Company Accounting Oversight Board (the PCAOB) has instituted as I feel a mutual responsibility to the integrity of the services I provide to both my clients directly and the protection of the general public as it relates.

I am committed to continual improvements in my audit quality. The inspection processes of both the CPCAF chapter of the AICPA Peer Review program and the PCAOB addresses this directly and is a positive means for feedback that will assist in the continuous improvement of the process.

I respect the processes and also understand the inspection may only take into account some of the work of the auditor and might not take into account the complete auditor quality processes that the practitioner provides.

This letter provides our response & actions to matters identified in Part I & II.

**ISSUER A:**

**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 audit deficiencies. The deficiencies identified in the audit reviewed included a deficiency of such significance that it appeared to the inspection team that the firm did not obtain competent evidential matter to support its opinion on the issuer's financial statement. That deficiency was the failure to perform sufficient audit procedures to evaluate the appropriateness of the issuer's accounting related to the conversion of debt to common stock.

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June 30, 2008

Mr. George H. Diacont, Director  
Public Company Accounting Oversight Board

**RESPONSE & ACTION:**

**A. Review of Audit Engagement – Insufficiently Supported Audit Opinion and Conversion of Debt to Common Stock Issue.**

The auditor acknowledges that a proposed an adjusting journal entry which would have recorded the beneficial conversion feature at the date of issuance not the date of conversion should have been submitted to the issuer. However, since the losses as presented to the auditor were overstated, the auditor considered this be a conservative presentation, protecting the shareholders by not overstating equity or income and did not propose an adjustment.

Despite this, after the inspection was completed, the auditor was instructed to have the issuer restate the financial statement results. The auditor successfully performed this during the 2007 year end audit. In addition, that audit was performed after the auditor disengaged with the issuer during 2007 and was subsequently engaged by a new board and management of the issuer in 2008.

The auditor could not supply the inspection team at the time with the work paper which contained the stock price for Issuer A the date of the conversion of the beneficial conversion feature. The auditor did have and did use such stock price table. This and the related audit work paper are enclosed with the response letter.

Based on the finding of the PCAOB inspection the auditor did remediate the beneficial conversion feature financial statement amendment with the issuer at the time of the December 31, 2007 audit. Issuer A did restate such.

**B. Issues Related to Quality Controls – Audit Performance**

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 non public portion of this report and will remain non public unless Firm fails to address them to the Board's satisfaction within 12 months of the date of this report.

**RESPONSE & ACTION:**

**B. Review of Quality Control**

- a. Technical Competence, Due Care and Professional Skepticism

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June 30, 2008

Mr. George H. Diacont, Director  
Public Company Accounting Oversight Board

**B. Review of Quality Control (cont'd)**

b. Technical Competence, Due Care and Professional Skepticism

The auditor regularly attends various CPE classes particularly for audit workpapers, procedures and FASB updates as well as PCAOB CPE seminars in Washington DC and consistently works towards meeting all the new and existing PCAOB and AICPA, Quality Control Procedures and Requirements (formal firm policy file is enclosed).

As a new publically registered auditor the auditor was keenly aware of the initial PCAOB application process and initiated a web based group audit email process whereby the auditor communicated a variety of quality control specifics geared towards the respect and importance of independence, integrity and objectivity, engagement performance, personnel management, acceptance and continuance of clients and engagements and finally the monitoring of such. In addition, the auditor developed and maintains an audit library as well as licensed electronic software using tools such as Thompson's PPC.

The auditor engages independent practitioners to perform and also assist in work paper preparation as well as engages an independent concurrent reviewer for a public audit engagement. In addition, the auditor engages other independent parties, where necessary, for various review work of all public audits.

c. Engagement Completion Document - The firm utilized written communication in both hard copy and a great deal of electronic correspondence to all on the audit committee. The documentation of such might have been overlooked by the inspection team as they might not have opened all the files as they were in "PFC" (personal filing cabinet) format. The auditor listed this in the actual complete audit work paper file as stated "The auditor considers the chronological e-mail correspondence file as an integral part of the audit." All documentation is attached and available.

d. Auditor Communications – Same answer as in (b) above.

The auditor has embraced and welcomed the inspection process of both the PCAOB inspection team and most recently Peer Review. As a conclusion to my response I am committed to utilizing this review process to apply, enhance, upgrade and perform to a maximum the proper procedures, where applicable. I am also committed to working the PCAOB staff to improve my system of quality control.

Thank you for your diligent inspection and consideration in this matter.

Respectfully submitted,

Michael F. Albanese, CPA