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**Report on**  
**2008 Inspection of McGladrey & Pullen, LLP**  
**(Headquartered in Bloomington, Minnesota)**

**Issued by the**  
**Public Company Accounting Oversight Board**  
**May 6, 2009**

**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**



Public Company Accounting Oversight Board

### **Preface to Reports Concerning Annually Inspected Firms**

The Sarbanes-Oxley Act of 2002 requires the Public Company Accounting Oversight Board ("PCAOB" or "the Board") to conduct an annual inspection of each registered public accounting firm that regularly provides audit reports for more than 100 issuers. The Board's report on any such inspection includes this preface to provide context for information in the public portion of the report.

A Board inspection includes, among other things, a review of selected audits of financial statements and of internal control over financial reporting. If the Board inspection team identifies deficiencies in those audits, it alerts the firm to the deficiencies during the inspection process. Deficiencies that exceed a certain significance threshold are also summarized in the public portion of the Board's inspection report. The Board encourages readers to bear in mind two points concerning those reported deficiencies.

First, inclusion in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the firm's attention. Under PCAOB standards, a firm must take appropriate action to assess the importance of the deficiency to the firm's present ability to support its previously expressed audit opinions. Depending upon the circumstances, compliance with these standards may require the firm to perform additional audit procedures, or to inform a client of the need for changes to its financial statements or reporting on internal control, or to take steps to prevent reliance on previously expressed audit opinions. A Board inspection does not typically include review of a firm's actions to address deficiencies identified in that inspection, but the Board expects that firms are attempting to take appropriate action, and firms frequently represent that they have taken, are taking, or will take, action. If, through subsequent inspections or other processes, the Board determines that the firm failed to take appropriate action, that failure may be grounds for a Board disciplinary sanction.

Second, the Board cautions against drawing conclusions about the comparative merits of the annually inspected firms based on the number of reported deficiencies in any given year. The total number of audits reviewed is a small portion of the total audits performed by these firms, and the frequency of deficiencies identified does not necessarily represent the frequency of deficiencies throughout the firm's practice. Moreover, if the Board discovers a potential weakness during an inspection, the Board may revise its inspection plan to target additional audits that may be affected by that weakness, and this may increase the number of deficiencies reported for that firm in that year. Such weaknesses may emerge in varying degrees at different firms in different years.



Public Company Accounting Oversight Board

#### **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.



## **2008 INSPECTION OF McGLADREY & PULLEN, LLP**

In 2008, the Board conducted an inspection of McGladrey & Pullen, LLP ("McGladrey" or "the Firm"). The Board is today 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, Appendix B, and portions of Appendix C. Appendix B provides an overview of the inspection process. Appendix C includes 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 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") performed an inspection of the Firm from August 2008 to December 2008. The inspection team performed field work at the Firm's National Office and at eight of its approximately 83 U.S. practice offices.<sup>3/</sup>

Board inspections are designed to identify and address weaknesses and deficiencies related to how a firm conducts audits.<sup>4/</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. Appendix B to this report provides a description of the steps the inspection team took with respect to the review of audits and the review of certain firm-wide quality control processes, along with a brief description of the Alternative Practice Structure ("APS") in which McGladrey is a participant.

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.

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<sup>3/</sup> This represents McGladrey's total number of practice offices; however, only approximately 38 of the Firm's practice offices have primary responsibility for issuer audit clients.

<sup>4/</sup> This focus on weaknesses and deficiencies 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.

<sup>5/</sup> When the Board becomes aware 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.

Accordingly, a Board inspection report should not be understood to provide any assurance that the firm's audits, or its issuer clients' financial statements or reporting on internal control, 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 selected audits performed by the Firm. Those audits and aspects were selected according to the Board's criteria, and the Firm was not allowed an opportunity to limit or influence the selection process.

In reviewing the audits, the inspection team identified matters that it considered to be audit deficiencies.<sup>6/</sup> Those deficiencies included failures by the Firm to perform, or to perform sufficiently, certain necessary audit procedures.

In some cases, the conclusion that the Firm failed to perform a procedure may be based on the absence of documentation and the absence of persuasive other evidence, even if the 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.<sup>7/</sup> 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.

When audit deficiencies are identified after the date of the audit report, PCAOB standards require a firm to take appropriate actions to assess the importance of the

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<sup>6/</sup> The discussion in this report of any deficiency observed in a particular audit reflects information reported to the Board by the inspection team and does not reflect any determination by the Board as to whether the Firm has engaged in any conduct for which it could be sanctioned through the Board's disciplinary process.

<sup>7/</sup> See AS No. 3, paragraph 9; Appendix A to AS No. 3, paragraph A28.

deficiencies to the firm's present ability to support its previously expressed opinions,<sup>8/</sup> and failure to take such actions could be a basis for Board disciplinary sanctions. In response to the inspection team's identification of deficiencies, the Firm, in some cases, performed additional procedures or supplemented its work papers.<sup>9/</sup>

In some cases, the deficiencies identified were of such significance that it appeared to the inspection team that the Firm, at the time it issued its audit report, had not obtained sufficient competent evidential matter to support its opinion on the issuer's financial statements. The deficiencies that reached this degree of significance are described below, on an audit-by-audit basis.

#### Issuer A

In this audit, the Firm failed in the following respects to obtain sufficient competent evidential matter to support its audit opinion –

- The Firm failed to perform sufficient procedures concerning the valuation of the issuer's investment securities. Specifically -
  - In connection with the Firm's testing of the valuation of certain difficult to value investment securities during interim audit procedures, the Firm retained a specialist to estimate the fair value of the securities. The specialist's initial fair value estimates were significantly lower than the issuer's recorded values. The specialist later increased its fair value estimates, though they remained significantly lower than the recorded values. Although the Firm used the specialist's work as evidence in the

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<sup>8/</sup> See AU 390, *Consideration of Omitted Procedures After the Report Date*, 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), and PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That is Integrated With an Audit of Financial Statements* ("AS No. 5"), ¶ 98.

<sup>9/</sup> The Board inspection process generally did not include review of such additional procedures or documentation, or of such revised accounting, although future Board inspections of the Firm may, as appropriate, include further review of any of these matters.

Firm's interim audit procedures, the Firm failed to (i) obtain an understanding of the valuation methods and assumptions used by the Firm's specialist to value the securities; and (ii) evaluate whether the specialist's findings supported the related investment securities valuation assertion. Further, the Firm did not obtain an understanding of the reason for the changes from the specialist's initial fair value estimates. Also, the Firm failed to perform audit procedures to provide a reasonable basis for extending its conclusions regarding the valuation of investment securities reached at an interim date to year end.

- In evaluating management's conclusion that the impairment of certain available for sale securities was temporary, the Firm failed to assess what a reasonable period of time would be for the securities to recover their values.
- The Firm failed to perform sufficient audit procedures related to the allowance for loan losses ("ALL"). Specifically –
  - The Firm failed to sufficiently evaluate the reasonableness of specific impairment reserves in that, other than reading a third party loan review report concerning one loan and verifying that the suggested reserve on that loan was recorded, the Firm performed no procedures to evaluate the reasonableness of specific impairment reserves.
  - During year-end audit procedures, the Firm identified as an error that the issuer's year-end loan loss factors were not directionally consistent with negative trends in past due loans, classified loans, and overall economic factors since the Firm's procedures at an interim date. The Firm concluded, however, that this error was offset by the effect of an aspect of the issuer's methodology for determining the historical loss component of its loan loss factors that the Firm viewed as inappropriate – specifically, that the methodology used historical loss rates of a peer group rather than the issuer's own loss rates, which were lower than the peer group's. The Firm concluded that the effect of this inappropriate aspect of the methodology offset the identified error, even though the Firm performed no procedures to quantify the effect of either that aspect of the methodology or the identified error, and even though the Firm had concluded in previous years and during

its interim audit procedures that the issuer's use of peer group loss rates, while inappropriate, still resulted in a reasonable estimate of the historical loss component.

**Issuer B**

The Firm failed to sufficiently evaluate the reasonableness of specific impairment reserves. The Firm selected the three largest impaired loans from the total impaired loan population to test. For one of those loans, the Firm failed to test the sources of data and evaluate the reasonableness of the assumptions that the issuer used to develop its fair value estimate. For the other two loans, the Firm used the work of a valuation specialist retained by the issuer, but failed to gain an understanding of the methods and assumptions used by the specialist. In addition, for the rest of the impaired loan population, the Firm's procedures were limited to a cursory review of a report on a portion of the impaired loan population to see whether any unusual items appeared.

**Issuer C**

In this audit, the Firm failed to perform sufficient procedures to test the issuer's ALL. The issuer had experienced significant credit quality deterioration during the fiscal year, particularly in its fourth quarter, and the Firm had concluded that significant deficiencies existed in the issuer's loan monitoring process. In applying loan review procedures to a sample of the issuer's non-homogenous loans, the Firm failed to determine its sample size based on relevant risks, and the sample of loans selected was not representative of the population because the selection was made from only "higher balance" loans. As a result, the audit procedures were not effectively designed to achieve the objectives of evaluating whether the issuer had identified the loans that should be considered to be classified loans.

**Issuer D**

In this audit, the Firm failed to sufficiently evaluate whether revenue from fixed price revenue arrangements was recognized appropriately. Specifically, while the Firm reviewed a significant fixed price revenue contract, the Firm failed to identify and consider all of the contractual terms that the Firm needed to consider in order to adequately assess the issuer's recognition of revenue from the contract. In addition, for the issuer's other fixed price revenue arrangements, the Firm failed to perform any

substantive procedures to identify and consider the contractual terms that the Firm needed to consider in order to adequately assess the issuer's recognition of revenue.

**Issuer E**

In this audit, the Firm failed in the following respects to obtain sufficient competent evidential matter to support its audit opinion –

- For accounts receivable, the Firm sent confirmation requests to customers for a sample of unpaid invoices; however, the Firm's sample size was insufficient to achieve the necessary level of assurance. Although the Firm assessed the control risk relating to the existence of accounts receivable as moderate, the Firm determined the sample size for confirmations of accounts receivable using a formula that assumed a lower level of risk. Additionally, the Firm's sample size was influenced by an expectation that analytical procedures would provide additional audit evidence, but those analytical procedures were inadequate as substantive tests because the Firm's expectations were not sufficiently precise to provide the necessary degree of assurance.
- The Firm failed to perform sufficient procedures to test the existence of revenue. Analytical procedures served as the Firm's primary substantive test of the existence of revenue. Those procedures were inadequate, however, in that the threshold that the Firm set for the amount of difference from expectation that could be accepted without further investigation allowed some such differences to go uninvestigated even though they exceeded materiality thresholds that the Firm had set for purposes of planning the audit.

**Issuer F**

In auditing the issuer's ALL, the Firm used the work of the issuer's personnel who perform credit reviews ("credit review function"), but failed to perform procedures to determine the extent to which it would be appropriate to do so. First, the Firm failed to gain a sufficient understanding of the credit review function. For example, the Firm failed to determine the extent to which the credit review function's procedures provided coverage of the issuer's loan portfolio, and the Firm failed to realize that the loan summaries used by the credit review function as the basis for testing the loan grades were prepared by issuer personnel responsible for initially assigning the loan grades. Second, the Firm failed to gain an understanding of the credit review function's findings

(e.g., level of loan grade classification changes) that may have warranted modification to the nature, timing and extent of the Firm's planned audit procedures.

**Issuer G**

In this audit, the Firm failed in the following respects to obtain sufficient competent evidential matter to support its audit opinion –

- The Firm failed to perform sufficient audit procedures relating to certain revenue. The analytical procedures that the Firm used for its primary test of certain revenue were inadequate as substantive tests because the Firm failed to develop expectations that were precise enough to provide the appropriate level of assurance that differences suggesting potential material misstatements, individually or in the aggregate, would be identified. In addition, the Firm failed to obtain corroboration of management's explanations of significant unexpected differences.
- The issuer acquired certain assets and liabilities of two entities. For both acquisitions, the Firm failed to evaluate whether the issuer properly recorded all identifiable intangible assets acquired. In addition, the Firm failed to evaluate whether the issuer's use of the straight-line method of amortization for customer-related intangible assets acquired in one of the acquisitions reflected the pattern in which the economic benefits of the intangible asset were being consumed. The Firm also failed to test the accuracy of the purchase price recorded for one of the acquisitions by, for example, comparing the amount to an executed purchase and sale agreement or verify the amount paid to the seller.

**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 and the following six functional areas (1) tone at the top; (2) practices for partner evaluation, compensation, admission, assignment of responsibilities, and disciplinary actions; (3) independence implications of non-audit services; business ventures, alliances, and arrangements; personal financial interests; and commissions and contingent fees; and the alternative practice structure; (4) practices for client acceptance and retention; (5) practices for consultations on

accounting, auditing, and SEC matters; and (6) the Firm's internal inspection program. 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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May 6, 2009  
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PART II, PART III, AND APPENDIX A OF THIS REPORT ARE NONPUBLIC  
AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

## **APPENDIX B**

### **The Inspection Process**

The inspection process was designed and performed to provide a basis for assessing the degree of compliance of the Firm with applicable requirements related to auditing issuers. This process included reviews of components of selected issuer audits completed by the Firm. These reviews were intended both to identify deficiencies, if any, in those components of the audits and to determine whether the results of those reviews indicated deficiencies in the design or operation of the Firm's system of quality control over audits. In addition, the inspection included reviews of policies and procedures related to certain functional areas of the Firm that could be expected to influence audit quality.

#### **1. Review of Selected Audits**

The inspection team reviewed aspects of selected audits, which it chose according to the Board's criteria. The Firm was not allowed an opportunity to limit or influence the engagement selection process or any other aspect of the review.

For each audit engagement selected, the inspection team reviewed the issuer's financial statements and certain SEC filings. The inspection team selected certain higher-risk areas for review and inspected the engagement team's work papers and interviewed engagement personnel regarding those areas. The areas subject to review included, but were not limited to, revenues, fair value, financial instruments, income taxes, reserves or estimated liabilities, inventories, consideration of fraud, and assessment of risk by the engagement team. The inspection team also analyzed potential adjustments to the issuer's financial statements that had been identified during the audit but not recorded in the financial statements. For certain selected engagements, the inspection team reviewed written communications between the Firm and the issuer's audit committee. With respect to certain engagements, the inspection team also interviewed the chairperson of the issuer's audit committee. In addition, the inspection team conducted focused inspections of audits of certain issuers whose audits had been reviewed during previous PCAOB inspections of the Firm to ascertain whether the audit procedures in areas with previous deficiencies had been improved.

When the inspection team identified a potential issue, it discussed the issue with members of the engagement team. If the inspection team was unable to resolve the

issue through this discussion and any review of additional work papers or other documentation, the inspection team issued a comment form on the matter and the Firm provided a written response to the comment form.

**2. Implementation of AS No. 5**

Shortly after the approval of AS No. 5, members of the Board's Office of the Chief Auditor and of the Division of Registration and Inspections reviewed documentation of the Firm's initial approach to the implementation of AS No. 5 and provided feedback to the Firm's National Office. Field inspection procedures in this area began with discussions with members of the Firm's leadership to address specific areas of inspection emphasis and the appropriate use of auditor judgment, and to outline planned communications with the Firm. The reviews of certain audits included discussions with engagement teams and the review of documentation regarding the following aspects of the Firm's audit of internal control over financial reporting: (1) risk assessment; (2) risk of fraud; (3) entity-level controls; (4) the nature, timing, and extent of tests of controls; and (5) evaluating and reporting deficiencies. The inspection team discussed its observations about the effectiveness of the implementation of AS No. 5 with the engagement teams, with emphasis on areas where implementation could be improved in subsequent audits. Periodically the observations were summarized and discussed with the Firm's National Office.

**3. Review of Certain Firm-Wide Quality Control Processes**

The inspection team reviewed certain Firm-wide quality control processes both to identify possible defects in the Firm's system of quality control and, where applicable, to update the Board's knowledge of the Firm's policies and procedures in those areas.

As reflected in the descriptions that follow, the inspection team's procedures took account of the fact that McGladrey is part of an APS with H&R Block, Inc. ("H&R Block"). H&R Block, through its wholly-owned subsidiary, RSM McGladrey Business Services, Inc., owns the non-attest businesses and assets of many certified public accounting firms, including RSM McGladrey, Inc. ("RSMI"). RSMI performs accounting, tax, and consulting services for corporate clients. McGladrey performs audits and other attest services. H&R Block does not have an ownership interest in McGladrey; however, RSMI provides working capital financing to McGladrey under a loan agreement, and the partners of McGladrey are employed as managing directors of RSMI. In addition, through an administrative services agreement, RSMI provides accounting, payroll, human resources, and other services to McGladrey and receives a

management fee for these services. As a consequence, the inspection procedures included interviews with certain personnel of RSMI.

a. Review of Partner Evaluation, Compensation, Admission, Assignment of Responsibilities, and Disciplinary Actions

The objective of the inspection procedures was to assess whether the design and application of the Firm's processes related to partner evaluation, compensation, admission, assignment, termination, and disciplinary actions could be expected to encourage an appropriate emphasis on audit quality and technical competence, as compared to marketing or other activities of the Firm. The inspection team interviewed members of the Firm's and RSMI's leaderships, as well as audit partners in practice offices, regarding these topics. In addition, the inspection team reviewed a sample of partners' personnel files, including files of partners who resigned or took early retirement, partners who had significant negative inspection results from recent internal, PCAOB, and peer-review inspections, and partners who received bonus compensation. Also, the inspection team interviewed audit partners regarding their time and responsibilities and interviewed practice office leadership regarding the performance of partners being inspected, the evaluation and compensation process, any disciplinary actions, and any situations where client management requested a change in the lead audit partner.

b. Review of Independence Policies and the Alternative Practice Structure

The objective of the inspection procedures in this area was to evaluate the Firm's policies and procedures for compliance with the independence requirements applicable to its audits of issuers. To accomplish this objective, the inspection team reviewed the Firm's policies, procedures, and guidance; reviewed the Firm's monitoring of compliance with its policies and procedures; reviewed information concerning the Firm's existing business ventures, alliances, and arrangements, as well as the Firm's process for establishing such enterprises; interviewed numerous National Office and practice office personnel regarding the Firm's independence policies, practices, and procedures; and, for a sample of the audits reviewed, tested compliance with the Firm's policies and applicable independence requirements.

The objectives of the inspection procedures in this area also included gaining an understanding of McGladrey's APS relationship with H&R Block and certain of its subsidiaries. The inspection team focused on independence issues related to the

provision of non-audit services to issuer clients; whether the personnel of H&R Block and its subsidiaries were familiar with the applicable policies and procedures regarding independence, integrity, and objectivity; and whether H&R Block has implemented an appropriate system of quality controls to ensure compliance with such policies and procedures. The inspection team reviewed, analyzed, and evaluated McGladrey's and RSMI's policies, procedures, and guidance materials related to independence (including independence consultations) for non-audit services to audit clients; their training programs on independence; and their procedures for independence consultations, which included reviewing the results of a sample of independence inquiries.

c. Review of Client Acceptance and Retention Policies

The objectives of the inspection procedures in this area were to evaluate whether the Firm appropriately considers and addresses the risks involved in accepting and retaining clients in the particular circumstances. Toward those objectives, the inspection team reviewed the Firm's policies, procedures, and forms related to client acceptance and continuance; interviewed members of the Firm's leadership; and for a sample of the engagements reviewed, assessed whether the audit procedures included the specific actions, if any, contemplated in response to any risks identified in the client acceptance or retention process.

d. Review of Practices for Consultations

The objective of the inspection procedures in this area was to assess the effectiveness of the Firm's consultation process. Toward this objective, the inspection team gained an understanding of and evaluated the Firm's policies and procedures relating to its consultation process, and reviewed a sample of consultations that occurred during the inspection period to evaluate the Firm's compliance with its policies and procedures, whether the conclusions were in accordance with professional standards, and whether the engagement teams acted in accordance with the conclusions.

e. Review of Internal Inspection Program

The objective of the inspection procedures in this area was to evaluate the effectiveness of the Firm's internal inspection program in enhancing audit quality. To meet this objective, the inspection team reviewed policies, procedures, guidance, and forms; documentation of the results of the current year's internal inspection program; and steps the Firm took in response to those results. The inspection team also

interviewed the Firm's leadership concerning the process and effectiveness of its internal inspection program. In addition, the inspection team reviewed certain audits that the Firm had inspected and compared its results to those from the internal inspection.

f. Review of Tone at the Top

The objective of the review of the Firm's "tone at the top" was to assess whether actions and communications by the Firm's and RSMI's leaderships demonstrate a commitment to audit quality. Toward that end, the inspection team interviewed members of the Firm's national, regional, and local, and RSMI's leaderships to understand their perspectives on the Firm's culture and the messages being conveyed by leadership. The inspection team also interviewed certain audit partners and managers to obtain their perspectives on communications from the Firm's and RSMI's leaderships. In addition, the inspection team reviewed the Firm's code of conduct; documents relating to measuring and monitoring audit quality; descriptions of the duties of, and relationships between and among, staff and leadership; results of surveys of staff; public company audit proposals; internal and external communications from management; descriptions of the Firm's financial structure and business plan; and agendas and minutes of the Firm's board of directors.

## APPENDIX C

### 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>10/</sup>

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<sup>10/</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.

# McGladrey & Pullen

Certified Public Accountants

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April 23, 2009

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

Re: Response to the Public Company Accounting Oversight Board (PCAOB) Report of 2008 Inspection of  
McGladrey & Pullen, LLP

Dear Mr. Diacont:

Thank you for the opportunity to submit our response to the PCAOB's March 27, 2009 draft of its Report of Inspection of McGladrey & Pullen, LLP. We support the PCAOB's inspection process and believe that inspection comments and observations will help us enhance the quality of audit engagements. McGladrey & Pullen is committed to using the inspection comments and observations to improve our system of quality controls. We have a long history of audit quality founded on our commitment to integrity, objectivity and excellence.

We have taken appropriate actions to address the deficiencies identified by the PCAOB's inspection team, including, in certain instances, performing additional procedures in accordance with AU 390, *Consideration of Omitted Procedures after the Report Date* and, in other instances, adding currently dated documentation to our workpapers to more completely and accurately describe the procedures performed, evidence obtained and conclusions reached. We note that none of the inspection comments resulted in the restatement of financial statements.

Please contact Bruce Webb, Executive Partner at (515) 281-9240 with any questions regarding this letter.

Sincerely,

*McGladrey & Pullen, LLP*