

**Inspection of  
Richard L. Brown & Company, P.A.  
(Headquartered in Tampa, Florida)**

**Issued by the  
Public Company Accounting Oversight Board  
May 21, 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**



### **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 RICHARD L. BROWN & COMPANY, P.A.

The Public Company Accounting Oversight Board ("PCAOB" or "the Board") has conducted an inspection of the registered public accounting firm Richard L. Brown & Company, P.A. ("the Firm"). The Board is issuing this report of that inspection in accordance with the requirements of the Sarbanes-Oxley Act of 2002 ("the Act").

The Board is making portions of the report publicly available. Specifically, the Board is releasing to the public Part I of the report and portions of Part IV of the report. Part IV of the report consists of the Firm's comments, if any, on a draft of the report.<sup>1/</sup>

The Board has elsewhere described in detail its approach to making inspection-related information publicly available consistent with legal restrictions.<sup>2/</sup> A substantial portion of the Board's criticisms of a firm (specifically criticisms of the firm's quality control system), and the Board's dialogue with the firm about those criticisms, occurs out of public view, unless the firm fails to make progress to the Board's satisfaction in addressing those criticisms. In addition, the Board generally does not disclose otherwise nonpublic information, learned through inspections, about the firm or its clients. Accordingly, information in those categories generally does not appear in the publicly available portion of an inspection report.

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<sup>1/</sup> The Board does not make public any of a firm's comments that address a nonpublic portion of the report unless a firm specifically requests otherwise. In addition, pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(b), if a firm requests, and the Board grants, confidential treatment for any of the firm's comments on a draft report, the Board does not include those comments in the final report at all. The Board routinely grants confidential treatment, if requested, for any portion of a firm's response that addresses any point in the draft that the Board omits 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 primary procedures for the inspection from August 6, 2007 to August 17, 2007. These procedures were 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 (Tampa, Florida) |
| Ownership structure                          | Corporation        |
| Number of partners                           | 1                  |
| Number of professional staff <sup>3/</sup>   | 3                  |
| 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.<sup>5/</sup> To achieve that goal, Board

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<sup>3/</sup> "Professional staff" includes all personnel of the Firm, except partners or shareholders and administrative support personnel. The number of partners and professional staff is provided here as an indication of the size of the Firm, and does not necessarily represent the number of the Firm's professionals who participate in audits of issuers or are "associated persons" (as defined in the Act) of the Firm.

<sup>4/</sup> The number of issuer audit clients shown here is based on the Firm's self-reporting and the inspection team's review of certain information for inspection planning purposes. It does not reflect any Board determination concerning which, or how many, of the Firm's audit clients are "issuers" as defined in the Act. In some circumstances, a Board inspection may include a review of a firm's audit of financial statements of an issuer that ceased to be an audit client before the inspection, and any such former clients are not included in the number shown here.

<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.

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.<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 Engagements

The inspection procedures included a review of aspects of the Firm's auditing of financial statements of two 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.<sup>7/</sup> The deficiencies identified in both of the audits reviewed included deficiencies of such significance that it appeared to the inspection team that the Firm did not obtain sufficient

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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.

competent evidential matter to support its opinion on the issuer's financial statements.<sup>8/</sup>  
Those deficiencies were –

- (1) the Firm's failure to identify, or to address appropriately, a departure from GAAP that related to a potentially material misstatement in the audited financial statements concerning the classification of non-cash transactions in the statement of cash flows;
- (2) the failure to perform audit procedures to evaluate the fair value of share-based payment transactions for services; and
- (3) the failure to perform sufficient audit procedures to test the valuation of inventory.

#### 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

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<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 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.



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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PARTS II AND III OF THIS REPORT ARE NONPUBLIC  
AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

**PART IV**

**RESPONSE OF THE FIRM TO DRAFT INSPECTION REPORT**

Pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(a), the Firm provided a written response to a draft of this report. Pursuant to section 104(f) of the Act and PCAOB Rule 4007(b), the Firm's response, minus any portion granted confidential treatment, is attached hereto and made part of this final inspection report.<sup>9/</sup>

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<sup>9/</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.

# RICHARD L. BROWN & COMPANY, PLLC

CERTIFIED PUBLIC ACCOUNTANTS

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April 17, 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 Public Company Accounting Oversight Board (PCAOB)  
Report of 2007 Inspection of Richard L. Brown & Company, P.A.

Dear Mr. Diacont:

Thank you for the opportunity to review the PCAOB's Draft Report on the 2007 Inspection of Richard L. Brown & Company dated March 20, 2009. We support the mission of the PCAOB, and we believe the inspections conducted by the PCAOB serve to effectively oversee and improve the audit quality of member firms.

The PCAOB inspection identified three deficiencies during its review of the selected engagements, which have been included in Part 1 of the PCAOB inspection report. The PCAOB findings relate to the sufficiency of competent evidential matter obtained to support the opinions on the issuer's financial statements. We believe, in each case, sufficient audit procedures were performed by us to support our opinion on the issuer's financial statements; however, we also agree that our audit work paper documentation could be improved. It should also be recognized that the sufficiency of competent evidential matter required to support an informed audit opinion is determined through the exercise of the auditor's professional judgment after a careful study of the particular circumstances.

## **With respect for the deficiencies described for Issuer A**

*The draft report states "the Firm's failure to identify, or to address appropriately, a departure from GAAP that related to a potential material misstatement in the audited financial statements concerning the classification of non-cash transactions in the statement of cash flows."*

## **Firm Response**

With one exception, the presentation of the Statement of Cash Flows for Issuer A is correct and in compliance with SFAS No. 95. Issuer A conducted a significant portion of their business

through an agent who used “a short-cut” process obtaining cash on Issuer A’s behalf and paying service providers and suppliers directly. Issuer A was short of staff and utilized the staff of the agent to help conduct its affairs. Additionally, certain payments advanced by a related party and intended for Issuer A were instead paid directly to the agent. Such payments physically bypassed Issuer A and were not properly recorded on Issuer A’s books.

The debt conversion item relates to compensation of senior officials. The contract calls for this payment to be made in cash. However, it was subsequently satisfied with a debt instrument and was incorrectly recorded.

We disagree with this conclusion and request that it be removed. Each of the items cited are discussed in the identified section.

Item 1. Proceeds from advances from third parties

Issuer A properly included the cash advances generated on their behalf by their agent, the president and owner of the studio, which provided technical recording service, hiring talent and outside suppliers. All payments to these talent and service providers were made in cash. There were no stock issuances or notes given for any of these payments. The accounting for these transactions on Issuer A’s books should have been to record cash advances and a related liability. We discovered these transactions during our audit work and proposed the necessary journal entries to properly record the activity. To further prove the studio acted as an agent for Issuer A, the studio’s president and owner attended several monthly board meetings as a guest - January 6, 2006; February 1, 2006; March 16, 2006; April 13, 2006; May 5, 2006; May 31, 2006; June 29, 2006; July 28, 2006; August 15, 2006; September 14, 2006; October 26, 2006; January 4, 2007; February 1, 2007; and March 1, 2007. The minutes are included in our files.

The accounting for this transaction on the Issuers A’s books should have been to record the cash advance and liability under the terms of the line of credit it had with the studio, and to record the disbursement as production expenses. We agree with this treatment and it is adequately documented in our files.

Item 2. Proceeds from advance from related party

During the year ended December 31, 2006, a related party made six advances to Issuer A for a total of \$605,000. These advances were paid directly to the agent as a partial payment on the line of credit noted in Item 1 above. These transactions were an accounting error and should have been reported as a cash advance from the related party with a corresponding liability to the related party on Issuers A’s books. The line of credit reflected Issuers A’s debt to the studio and should have been reduced when the payments were subsequently made by the related party to the studio. We found two of the advances during our review of the Board of Director minutes and followed up with the president of the studio to determine how many advance were made and how much had been advanced by the related party. We then proposed an adjustment to record this amount on Issuer A’s books. These transactions are adequately documented in the 2006 audit files for Issuer A.

### Item 3. Proceeds from debt conversion

Issuer A included this item in its cash flows from investing activities. In essence, Issuer A and the CEO “swapped checks,” and as a result we treated this item as a source and use of cash. At that point in time Issuer A did not have sufficient cash resources to write this check. As a result, we now believe this item was a non-cash transaction.

*The draft report states, “The failure to perform audit procedure to evaluate the fair value of share-based payment transactions for services.”*

#### Firm Response

We disagree with this conclusion and request that it be removed.

Starting in 2001, Issuer A believed that the quoted market price of its shares did not reflect the fair market value as it relates to the issuance of shares for services. At the suggestion of our concurring partner at that time (a highly experienced auditor of public companies) we recommended that Issuer A determine the amount of the trading discount based on Issuer A’s historical data. The significant items that made up the discount are listed as follows:

1. Trading price is generally the purchase price. Anyone receiving and selling shares would only receive the selling price, a built in discount.
2. The seller incurred expenses in getting the shares into the hands of a broker and payment of selling commission. Issuer A found such trading expenses to be significant in certain cases due to the thinly traded nature of its stock and the dearth of brokers willing to trade shares of such thinly traded stock. Another built in discount.
3. Because Issuer A was using shares of its common stock to pay for goods and services, they were required to file a Form S-8. As each S-8 was filed the bid price of its shares dropped, significantly in most cases. By the time the supplier received the shares, transmitted them to the broker and sold them in the market place, the share value had dropped enough that the supplier received less cash than the fair value of his services.

As a result, in 2001, Issuer A adopted the discount trading market price method of calculating the per share value of shares to be issued for services.

#### GAAP

PPC Guide to GAAP 2007 – Section 50.230

“When an entity issues equity instruments to nonemployees in exchange for goods or services, the transaction should be accounted for based upon the fair value of the goods or services received or the fair value of the equity instrument, whichever can be more reliably measured.

Frequently, the fair value of goods or services received from suppliers can be reliably measured and therefore indicates the fair value of the equity instruments issued....”

Clearly, GAAP contemplates that Issuer A has the flexibility to determine the fair value of its equity instrument to be issued in payment for services. This accounting procedure was consistently followed by Issuer A for all years after 2001.

#### Audit Work Performed

We inquired of management whether or not the condition that caused the adoption of this accounting method still existed and if they had calculated the cost of shares issued consistently with prior years. We documented the results of that conversation. We then obtained a schedule of shares issued and tested the valuation of share amounts. We also agreed the number of shares to Board meetings and filings with the SEC. We also agreed the totals to contract or invoices from suppliers. No exceptions were noted.

For the record, we note that three different concurring partners, all with extensive SEC audit experience, understood exactly the accounting method that Issuer A had adopted and applied consistently, concurred with our approach to the audit testing and documentation. Further, this engagement was reviewed by PCAOB staff for the year ended December 31, 2003. These transactions were the subject of discussions with the inspectors. Your staff concurred with both Issuer A’s accounting treatment and the audit work performed. We performed and documented those same procedures each year thereafter, based on the results of our 2003 inspection where no comments were made.

#### **With respect for the deficiencies described for Issuer B**

*The draft report states, “The failure to perform sufficient audit procedures to test the valuation of inventory.”*

#### **Firm Response**

We disagree with this conclusion and request that it be removed.

During our initial audit of Issuer B as of and for the year ended December 31, 2004, Issuer B performed a complete count of all inventory on hand. We were on site during the counting process, performing our own test counts of parts and participated in a complete count of finished goods inventory. The finished goods inventory and parts inventory were stored in a locked facility, with access limited to only certain Issuer B employees. The inventory value was priced at both book value and at current replacement cost. The inventory was valued at substantially less than the replacement cost. We traced our test counts to the final inventory and tested Issuer B’s work on replacement value. We performed these same procedures again in 2005 and decided to limit our counts and procedures in 2006 because the inventory had not changed significantly and because Issuer B hired a laser specialist to conduct a study of their laser technology and the value of its inventory.

This study was conducted in early 2007, prior to the completion of our audit of Issuer B. At its conclusion, we had discussions with the specialist and were informed that the inventory had a sales value of \$6,000,000. The lasers had been and would be sold outside the US through its distributor network into the Dental Market. The CEO of Issuer B followed up with their distributors in the Middle East and China, both of whom were very interested. We were supposed to receive a copy of the report. As part of the PCAOB inspection, it came to our attention that we did not have a copy of the report in our files or document our discussion with the laser specialist. We requested a copy which was received after the conclusion of this inspection because the specialist who had the report was out of town at a technology conference. We were also told by Issuer B that a copy had been previously forwarded to us when it had been received from the specialist who had prepared the report. While reviewing our files to prepare our response to the PCAOB inspection, we found the original copy of the specialist's report, as forwarded to us by Issuer B, filed loosely in one of our permanent files. This report was received within 45 days of the date we granted permission to use our audit report and should have been included in our audit file in accordance with Auditing Standard No. 3. At the request of the inspection team we forwarded a copy for their review. We have added currently dated documentation to our workpapers to better support the procedures performed and have added the specialist's report to our audit files in accordance with AU 390, *Consideration of Omitted Procedures after the Report Date* and AU 336, *Using the Work of a Specialist*.

Based upon the additional audit procedures performed, no new information came to our attention that caused us to believe our previously issued audit reports should be withdrawn.

As a result of the PCAOB inspection, we have reassessed our quality control procedures and have made modifications to certain audit practices and procedures that address the items noted by the PCAOB, specifically related to improved documentation. These modifications will be discussed in a separate letter to the PCAOB Division of Registration and Inspections at a later date.

Richard L. Brown & Company is committed to achieving the highest level of audit quality. We appreciate the inspection team's efforts, and their courteous and professional manner in conducting the inspection. We recognize and appreciate the importance of the inspection process, and commit to enhancing our firm's quality control policies and procedures based on the findings of this inspection.

Sincerely,

*Richard L. Brown & Company*