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Report on

2010 Inspection of Deloitte & Touche LLP
(Headquartered in New York, New York)

Issued by the

Public Company Accounting Oversight Board

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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. 104-2011-290

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 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 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 financial statement misstatements, including failures to comply with 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 apparent misstatements 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 whether an issuer's financial statements are misstated or fail to comply with Commission disclosure requirements, rests with the Commission. Any description, in this report, of financial statement misstatements or failures to comply with 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.

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2010 INSPECTION OF DELOITTE & TOUCHE LLP

Preface

In 2010, the Public Company Accounting Oversight Board ("PCAOB" or "the Board") conducted an inspection of the registered public accounting firm Deloitte & Touche LLP ("Deloitte" or "the Firm") pursuant to the Sarbanes-Oxley Act of 2002 ("the Act").

The Board is issuing this report in accordance with the requirements of the Act.[1/] The Board is releasing to the public Part I of the report, Appendix C, and portions of Appendix D. Appendix C provides an overview of the inspection process for annually inspected firms.[2/] Appendix D includes the Firm's comments, if any, on a draft of the report.[3/] A substantial portion of the Board's criticisms of a firm (specifically criticisms of the firm's quality control system) is nonpublic, unless the firm fails to make sufficient progress in addressing those criticisms.

Board inspections are designed to identify and address weaknesses and deficiencies related to how a firm performs audit work.[4/] To achieve that goal, Board inspections include reviews of certain aspects of selected audit work performed by the firm and reviews of certain aspects of the firm's quality control system. It is not the

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1/ In its Statement Concerning the Issuance of Inspection Reports, PCAOB Release No. 104-2004-001 (August 26, 2004), the Board described its approach to making inspection-related information publicly available consistent with legal restrictions.

2/ The Act requires the Board to conduct an annual inspection of each registered public accounting firm that regularly provides audit reports for more than 100 issuers.

3/ 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.

4/ 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.

purpose of an inspection, however, to review all of a firm's audit work or to identify every respect in which reviewed audit work is deficient. Accordingly, a Board inspection report should not be understood to provide any assurance that the firm's audit work, or the relevant issuers' financial statements or reporting on internal control, are free of any deficiencies not specifically described in an inspection report.

If the Board inspection team identifies deficiencies that exceed a certain significance threshold in the audit work it reviews, those deficiencies are summarized in the public portion of the Board's inspection report.[5/] The Board cautions, however, against extrapolating from the results presented in the public portion of the report to broader conclusions about the frequency of deficiencies throughout the Firm's practice. Audit work is selected for inspection largely on the basis of an analysis of factors that, in the inspection team's view, heighten the possibility that auditing deficiencies are present, rather than through a process intended to identify a representative sample.

[5/] Inclusion of a deficiency in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the firm's attention. 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 deficiencies to the firm's present ability to support its previously expressed 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. The inspection team may review, either in the same inspection or in subsequent inspections, the adequacy of the firm's compliance with these requirements. Failure by a firm to take appropriate actions, or a firm's misrepresentations, in responding to an inspection report, about whether it has taken such actions, could be a basis for Board disciplinary sanctions.

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's staff ("the inspection team") conducted primary procedures for the inspection from October 2009 through March 2011. The inspection team performed field work at the Firm's National Office and at 36 of its approximately 66 U.S. assurance practice offices.

A. Review of Audit Engagements

The 2010 inspection of the Firm included reviews of aspects of 57 audits performed by the Firm and reviews of the Firm's audit work on one issuer audit engagement in which the Firm played a role but was not the principal auditor. The inspection team selected the audits and aspects to review, and the Firm was not allowed an opportunity to limit or influence the selections.

The inspection team identified matters that it considered to be deficiencies in the performance of the audit work it reviewed. Those deficiencies included failures by the Firm to identify, or to address appropriately, financial statement misstatements, including failures to comply with disclosure requirements,[6/] as well as failures by the Firm to perform, or to perform sufficiently, certain necessary audit procedures. In one instance, follow-up between the Firm and the issuer led to a change in the issuer's accounting. In some cases, the conclusion that the Firm failed to perform a procedure was based on the absence of documentation and the absence of persuasive other evidence, even if the Firm claimed to have performed the procedure.[7/]

The inspection team considered certain of the deficiencies that it observed to be audit failures. Specifically, certain of the identified deficiencies were of such

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[6/] 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 applicable accounting principles, the Board's practice is to report that information to the SEC, which has jurisdiction to determine proper accounting in issuers' financial statements.

[7/] PCAOB Auditing Standard No. 3, *Audit Documentation* 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.

significance that it appeared that the Firm, at the time it issued its audit report, had failed to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements and/or on the effectiveness of internal control over financial reporting ("ICFR"). In addition, one of the identified deficiencies, which occurred in an audit in which the Firm played a role but was not the principal auditor, was of such significance that it appeared to the inspection team that the Firm had not obtained sufficient appropriate audit evidence to fulfill the objectives of its role in the audit. The audit deficiencies that reached these levels of significance are described below.[8/]

1. Issuer A

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and the effectiveness of internal control over financial reporting ("ICFR"). Specifically –

- The Firm failed to perform sufficient procedures to test the design and operating effectiveness of two important review controls on which it relied in evaluating internal controls over a number of significant accounts, including revenue, accounts receivable, inventory, and certain accruals. Specifically, the Firm failed to gain an understanding of how the information used in the review controls was generated, to assess the design of the review and approval process, and to gain an understanding of the output from the process. Further, the Firm's tests of the operating effectiveness of the review controls were limited to reading notes of meetings to verify that the appropriate individuals attended the meetings and that certain account balances were discussed.

- The Firm failed to perform sufficient substantive procedures to test a number of significant accounts, including revenue, accounts receivable, inventory, and certain accruals as, in designing its substantive procedures, it relied on internal controls that it had not tested adequately, as discussed above. In addition, the Firm failed to test the completeness and accuracy of the computer-generated information that it used in its revenue testing.

- The Firm failed to perform sufficient procedures to test the existence of the issuer's inventory. The Firm performed physical inventory observations at approximately one-half of one percent of the issuer's locations during the first

[8/] 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.

half of the year, and used a substantive analytical procedure to test the year-end inventory balance. To develop its expectation of the year-end inventory balance, the Firm used the inventory balances from the small number of locations at which it had performed inventory observations during the first half of the year to predict the inventory balances for all the locations at the end of the year. The Firm, however, did not obtain evidence that the inventory balances at the issuer's retail locations were similar. In fact, there was considerable variation, approximately 15 percent, in the inventory balances at the three retail stores where physical inventories were observed. In addition, the Firm did not have evidence that the inventory balances in the first half of the year could be expected to be predictive of the balances at year end.

2. Issuer B

After the date of the issuer's balance sheet, but before the release of the Firm's audit opinion, the issuer reported that it anticipated that comparable store sales for the first quarter of the year would be significantly lower than those for the first quarter of the year under audit. The Firm had performed sensitivity analyses as part of its assessment of the issuer's evaluation of its compliance with its debt covenants, the issuer's ability to continue as a going concern, and the possibility of the impairment of the issuer's long-lived assets. The Firm failed to consider the implications of the anticipated decline in sales to its sensitivity analyses and its conclusions with respect to compliance with debt covenants, the issuer's ability to continue as a going concern, and impairment of long-lived assets.

3. Issuer C

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and the effectiveness of ICFR –

- The Firm failed to perform sufficient procedures to test the appropriateness of the issuer's recognition of revenue.
  - Most of the issuer's sales to its dealers were financed by lending institutions that had repurchase agreements with the issuer in the event of the dealer's default. The Firm failed to evaluate whether the ultimate collectability of these sales to dealers was reasonably assured.
  - The Firm failed to consider whether a portion of the sales proceeds representing the fair value of the repurchase agreements should have been allocated to deferred revenue.

  - The Firm failed to adequately evaluate the issuer's conclusion that sales to the issuer's largest dealer meet the criteria for revenue recognition. Specifically, the Firm failed to include in its evaluation certain key facts, such as an exclusivity agreement between the dealer and the issuer that required the dealer to purchase a significant portion of its overall product requirements from the issuer; loans made by the issuer to the owner of the dealer during the year with a requirement that the proceeds be contributed as additional capital to the dealer, with half of the proceeds being used to purchase product from the issuer; and guarantees that the issuer provided to the dealer's lenders.

- The Firm failed to adequately evaluate the reserve for losses from repurchase agreements because the Firm failed to evaluate whether the recent deterioration in the economic environment should have affected the issuer's reserve methodology, which was based only on historical results.

- The Firm failed to adequately evaluate whether the issuer should have consolidated the financial statements of its largest dealer, as it failed to consider certain of the issuer's potential variable interests in the dealer.

- The Firm failed to identify and test any controls over the issuer's evaluation of, and accounting treatment for, potential variable interests.

4. Issuer D

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and the effectiveness of ICFR –

- The Firm failed to perform sufficient procedures to test the issuer's evaluation of goodwill for impairment. Specifically –

  - The Firm failed to sufficiently evaluate the assumptions the issuer used in its revenue and expense projections, as the Firm limited its procedures to comparing current-year interim data to unaudited financial statements and verifying the mathematical accuracy of the projections. In addition, there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had evaluated the reasonableness of the risk premium that the issuer used to calculate the weighted average cost of capital, which was a significant assumption in the issuer's goodwill impairment analysis.

- The Firm failed to sufficiently test the issuer's model for developing the fair value estimate for the loan portfolio, which the issuer used in its goodwill impairment analysis, as the Firm:
    - Failed to perform any procedures beyond inquiry to gain an understanding of the model;
    - Failed to test the significant assumptions and data inputs used in estimating the fair value of the loan portfolio; and
    - Failed to take into account in its evaluation an analysis that the issuer had obtained from an outside party that indicated a significantly lower fair value for a substantial portion of the loan portfolio.

- The Firm failed to perform sufficient procedures to test the issuer's evaluation of possible other-than-temporary impairment ("OTTI") of its securities. Specifically, the Firm failed to test whether the issuer had subjected to an evaluation of OTTI all securities that should have been subjected to such an evaluation and failed to test the assumptions and calculations used in this evaluation.

- The Firm failed to obtain an understanding of the specific methods and assumptions underlying the fair value measurements obtained from pricing services and used in the Firm's testing of the fair value of the issuer's financial instruments without readily determinable fair values ("hard-to-value financial instruments").

- The Firm failed to sufficiently test the issuer's fair value disclosures. Specifically, the Firm failed to identify and test any controls over the issuer's process for identifying the level of the issuer's securities within the fair value hierarchy set forth in Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 820, *Fair Value Measurements and Disclosures* and to perform substantive procedures to test the issuer's classification of securities within that hierarchy.

- The Firm failed to perform sufficient substantive procedures to test the issuer's allowance for loan losses, as it designed its procedures based on a level of reliance on internal control that was excessive due to the deficiencies discussed below.

- The Firm failed to adequately test the issuer's controls over the estimation of the allowance for loan losses, as it failed to adequately test the monitoring process performed by the issuer's internal loan review function, an important

control over the accuracy of the loan risk ratings and the timely identification of problem loans. Specifically, the Firm did not test the determination and recording of loan risk ratings resulting from the issuer's internal loan review function and did not evaluate the internal loan reviewers' qualifications, objectivity, methodology, level of coverage, and findings.

5. Issuer E

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements –

- The issuer held land that had been subject to a purchase agreement whose closing date had been extended several times in recent years. During the year, the issuer obtained an appraisal of the land, which indicated a fair value of the land that was between 20 percent and 49 percent below the issuer's recorded value, or an approximate difference of between five and twelve times the Firm's established materiality level. The appraisal stated that a development project like the one contemplated by the anticipated buyer of the property probably would not be viable for several years. In estimating the fair value to report, the issuer gave a 50 percent weighting to an amount that was close to the highest value indicated in this appraisal, a 25 percent weighting to the price specified in the purchase agreement, and a 25 percent weighting to a price that it asserted was the lowest it would accept for the land. Both of these latter prices were significantly above the value indicated in the appraisal.

  The Firm's evaluation of the issuer's impairment analysis of this land held for sale did not sufficiently take into account the evidence (in the form of the appraisal) that indicated a lower fair value of the land than the issuer had recorded. The Firm accepted the issuer's decision to give significant weight to the two other scenarios described above, which (a) significantly increased the reported value of the land over that indicated by the recent appraisal, (b) in the case of one scenario, was based on management's representations (rather than market information), and (c) in the case of the other scenario, was based on the purchase agreement, which had been pending for several years and was based on a contemplated development project that the issuer's own specialist had stated may not be viable for several years.

- The Firm failed to perform sufficient procedures to evaluate the reasonableness of the revenue growth assumptions that the issuer used in its analyses of the potential impairment of goodwill and indefinite-lived intangible assets. Specifically, there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had considered the adverse

implications of industry forecasts that indicated annual declines in a key component of revenue, as opposed to the growth that the issuer projected.

6. Issuer F

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements –

- As part of its impairment analysis for goodwill, the issuer obtained from its external valuation specialist two estimates of the fair value of one of its reporting units; one estimate was based on a market approach, which was weighted 60 percent, and the other on an income approach, which was the higher amount and was weighted 40 percent. The Firm did not determine the reasons for the significant difference between the two estimates in order to evaluate whether one of the individual approaches or the weighted average was the best indicator of fair value. Further, the Firm failed to sufficiently evaluate the reasonableness of the revenue growth assumptions that were used in the income approach and that were significantly higher than the issuer's historical revenue growth rates. Specifically, the Firm's evaluation was limited to inquiry of management, review of certain long-term industry outlook reports that did not address the short-term growth rates used in the analyses, review of a few recent requests for proposals and long-term supply contracts that covered an insignificant portion of the projected revenue, and a comparison of the assumptions to those management used for other purposes.

- In its analysis of the possible impairment of long-lived assets for another reporting unit, the issuer developed a cash flow analysis using revenue growth rates that were significantly higher than its historical growth rates. The cash flow analysis was sensitive to small changes in the revenue growth assumptions. The Firm failed to perform sufficient procedures to evaluate the issuer's analysis, as the Firm's evaluation of the revenue growth assumptions was limited to comparing the revenue growth rates used in the analysis to those used by management for other purposes and calculating that the reporting unit's revenue backlog represented approximately ten percent of the next year's projected revenues. In addition, as part of its analysis, the issuer included a scenario that assumed it would sell the reporting unit. Under this scenario, the issuer allocated a portion of a nonbinding offer it had received for multiple reporting units to the reporting unit, but the Firm failed to evaluate the reasonableness of the issuer's allocation method.

7. Issuer G

In this audit, the Firm failed to perform sufficient procedures to test the assumptions underlying the valuation of certain of the issuer's inventory. The Firm selected a sample of items for testing from the issuer's population of inventory items for which an impairment charge had been recorded during the year. For all inventory items for which the issuer had not recorded an impairment charge during the year (which represented more than 90 percent of the carrying value of the inventory), however, the Firm selected only two items for testing.

8. Issuer H

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and the effectiveness of ICFR –

- The Firm failed to perform sufficient procedures to test an actuarially determined liability. Specifically, the Firm –
  - Failed to test the completeness and accuracy of the data used in the actuarial estimate;
  - Failed to obtain an understanding of the nature and weighting of two external data sets that the actuary used in the development of the estimate; and
  - Failed to sufficiently test controls over the data maintained by external administrators that were used in the determination of the liability. Specifically, the Firm failed to test controls at the issuer over the completeness and accuracy of the data maintained by one external administrator that would meet the user control objectives identified in the administrator's service auditor's report, and failed to obtain and review a service auditor's report regarding the effectiveness of another administrator's internal control or otherwise test the relevant controls.
- The Firm failed to perform sufficient procedures to test the valuation of the issuer's inventory. Specifically, the Firm –
  - Failed to sufficiently test a key component of the calculations that the issuer used to identify potential inventory impairment, as the Firm's substantive procedures were limited to comparing the key component information to other information that also was generated internally by the issuer, and this information was not tested substantively;

- Failed to sufficiently evaluate the reasonableness of the issuer's assertion that certain inventory was not impaired, as the Firm selected a sample for testing but failed to test the issuer's significant assumptions for a number of items within the sample; and

- Designed its substantive procedures based on a level of reliance on internal control that was excessive due to the deficiencies discussed below.

- The Firm excluded the inventory impairment computer application from its information technology general controls ("ITGCs") testing, and there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had tested controls over the completeness and accuracy of the data derived from this application that the issuer used in controls related to the evaluation of inventory for impairment.

9. Issuer I

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements –

- The Firm failed to perform sufficient procedures to evaluate the reasonableness of certain significant assumptions that the issuer used in its analyses of the potential impairment of certain of its goodwill and indefinite-lived intangible assets. Specifically, for certain reporting units, the Firm failed to evaluate the issuer's projected net sales growth, divisional operating profit, and capital expenditures and, for another reporting unit, the Firm's procedures to test these projections were limited to inquiries of management and reviewing management-prepared memoranda.

- The Firm failed to perform sufficient substantive procedures to test the valuation of the issuer's pension plan assets. The Firm designed its procedures based on a level of reliance on internal control that was excessive, due to its failure to identify and test any controls related to the pricing of investments at the individual asset level.

10. Issuer J

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements –

- The Firm failed to perform procedures, beyond inquiry at an interim date, to evaluate the reasonableness of certain of the key assumptions that the issuer used to identify and measure impairments of certain of its long-lived assets.

- The Firm failed to evaluate certain of the key assumptions and inputs that the issuer used in the calculation of a significant long-term liability.

11. Issuer K

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements –

- The Firm failed to perform sufficient procedures to test the completeness, existence, and valuation of inventory.

  - The Firm failed to perform sufficient substantive procedures related to inventory additions and inventory cutoff. The Firm designed its procedures based on a level of reliance on internal control that was excessive, because the Firm:

    - Failed to sufficiently test the operating effectiveness of an important manual control related to inventory costs, as it limited its procedures to a sample of one item;

    - Failed to test the design and operating effectiveness of an important control related to the capitalization of inventory costs; and

    - Failed to adequately test an important control related to the valuation of inventory, as it failed to test the data used in the calculation of a key component of the inventory-costing calculation.

  - The analytical procedure that the Firm used to test inventory valuation of real estate projects was not sufficiently precise to provide the necessary level of assurance, as it was performed collectively for two large groups of projects, rather than at a more disaggregated level such as, for example, at the level of the individual project, of which there were approximately 100.

  - The Firm failed to adequately test a significant adjustment to the issuer's inventory and cost of sales in that it tested only certain elements of the adjustment and limited its procedures on those elements to inquiry.

  - The Firm failed to adequately test the net realizable value of inventory, as its procedures were limited to inquiry of management.

- The Firm failed to sufficiently evaluate the appropriateness of the issuer's revenue and expense recognition related to customer incentive plans, in that it failed to evaluate whether the method the issuer used to recognize deferred revenue was representative of when revenue was earned, and it failed to test whether the issuer's deferral of certain costs was appropriate by evaluating whether they were incremental as a result of the plans.

12. Issuer L

In this audit, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements –

- The Firm failed to perform sufficient substantive procedures to test certain accounts receivable and revenue. Specifically, the Firm –

  - Failed to sufficiently test the completeness and accuracy of the computer-generated information that it relied upon in its accounts receivable and revenue procedures, in that its testing was limited to reconciling the sub-ledger to the general ledger and to selecting one item for testing, even though it had concluded that the issuer's ITGCs were ineffective; and

  - Failed to test whether revenue was recognized in the appropriate period.

- The Firm failed to perform sufficient substantive procedures to test the existence, completeness, and valuation assertions related to significant amounts of inventory and cost of sales. Specifically, the Firm –

  - Failed to test the completeness and accuracy of certain computer-generated information that it relied upon in certain of its inventory and cost of sales audit procedures;

  - Failed to perform sufficient procedures to test the existence and completeness of certain inventory, because the Firm failed to select items to count from the issuer's computer-generated report of distributors' inventory and, in testing the issuer's cycle-counting procedures, selected only items from the issuer's count sheets for test-counting and selected only one day for testing, without a basis for doing so;

  - Failed (a) to evaluate the differences that it identified in its observations of inventory, beyond documenting its understanding of the issuer's process

for dealing with such differences; (b) to extend its tests of the valuation of inventory as a result of the differences it identified during its price-testing of the inventory or to project the results to the entire population; and (c) to use a sample size for testing the inventory reserves that was commensurate with its risk assessment; and

- Failed to perform sufficient procedures to extend to the year end the audit conclusions that it reached at the interim testing date (three months before year end), because the Firm limited its roll-forward procedures to comparing the net inventory balances at the interim date to those at the year end.

- The Firm failed to test the completeness and accuracy of the computer-generated information that it relied upon in its testing of the issuer's analyses of the potential impairment of goodwill and other indefinite-lived intangible assets.

13. Issuer M

In this audit, the Firm failed to perform sufficient procedures to evaluate the issuer's analysis of the possible impairment of goodwill for one reporting unit. Specifically, the Firm failed to evaluate the reasonableness of certain significant assumptions used in the issuer's discounted cash flow analysis, including projected improvements in gross margins and operating expense ratios, and certain cash flow adjustments. Further, the Firm failed to consider the implications of differences between the issuer's actual and previously projected revenue and income for the prior year. In addition, the Firm failed to evaluate the appropriateness of the issuer's decision to combine certain reporting units when evaluating whether an updated impairment test was required.

14. Issuer N

In this audit, the Firm failed to sufficiently test the valuation of the issuer's long-lived assets. Specifically, the Firm failed to identify and address the inconsistency between the issuer's exclusion of the carrying value of certain assets from the asset group being tested for impairment and the issuer's inclusion, in its projected cash flows, of the cash flows associated with those assets. In addition, the Firm failed to evaluate whether the issuer's decision not to test certain other assets for impairment was appropriate, even though the issuer's initial analysis of those assets indicated that their projected cash flows might be less than their carrying values.

15. Issuer O

In this audit, the Firm failed to perform sufficient substantive procedures to test the valuation of goodwill, as it designed its procedures based on a level of reliance on internal control that was excessive. The Firm failed to sufficiently test the design and operating effectiveness of important controls that addressed the valuation of goodwill. Specifically, the Firm failed to test control activities related to the issuer's budget, which was used in the controls over the valuation of goodwill, and failed to test the completeness and accuracy of the information the issuer used to develop the budget. In addition, the Firm failed to obtain evidence to support its conclusion that certain controls within the financial reporting process on which it relied operated at a level of precision that would prevent or detect a material misstatement.

16. Issuer P

The Firm failed to perform sufficient procedures to test the valuation of certain long-lived assets. Specifically, the Firm –

- Failed to evaluate the assumptions the issuer used to identify potentially impaired stores;

- Failed to test the completeness of the store-level financial data that the issuer used to evaluate potentially impaired stores;

- Failed to adequately test key assumptions the issuer used in the cash flow projections prepared for potentially impaired stores, in that the Firm limited its procedures to inquiry of management, recalculation, and comparison of the projections to an internally generated operations statement that the Firm did not test beyond inquiry;

- Failed to identify and address the inconsistency between the issuer's exclusion of the carrying value of certain assets from the asset group being tested for impairment and its inclusion, in its projected cash flows, of the cash flows associated with those assets; and

- Failed to test, beyond inquiry, the design and operating effectiveness of controls over the evaluation of long-lived assets for impairment.

In addition, the Firm failed to perform sufficient substantive procedures to test restructuring charges, as it designed its procedures based on a level of reliance on internal control that was excessive. The Firm failed to adequately test the design and operating effectiveness of important controls that addressed the valuation of the issuer's restructuring reserve and related expenses. Specifically, there was no evidence in the

audit documentation, and no persuasive other evidence, that the Firm had performed procedures to test the controls beyond observing signatures on certain documents evidencing the issuer's review.

17. Issuer Q

To evaluate the possible impairment of certain of its long-lived assets, the issuer prepared an undiscounted cash flow analysis for the assets, using revenue growth-rate assumptions that were substantially above the rates the issuer had experienced in recent years. The Firm failed to sufficiently evaluate the revenue growth-rate assumptions, in that the Firm's procedures to test them were limited to inquiry and consideration of an industry report. Further, the Firm failed to sufficiently evaluate the issuer's conclusion that there were no impairment indicators for another long-lived asset, as the Firm's testing was limited to inquiry and a consideration of current-year cash flows, despite the fact that significant growth in cash flows over the current year (the initial year of the use of the asset) would be required over the life of the asset in order for its recorded value to be fully recoverable.

18. Issuer R

The Firm failed to perform sufficient procedures to test the valuation assertion for finite-lived intangible assets. Specifically, the Firm failed to evaluate the issuer's decision not to evaluate whether its finite-lived intangible assets were impaired, even though the issuer had identified triggering events that required the issuer's indefinite-lived intangible assets to be tested for possible impairment. Further, the Firm failed to test the reasonableness of the remaining amortization period for the finite-lived intangible assets.

19. Issuer S

In this audit, the Firm failed to perform sufficient procedures to test revenue and cost of sales for a portion of the issuer's business. The Firm's testing of these accounts consisted of analytical procedures and tests of details. The Firm –

- Failed to sufficiently test the accuracy and completeness of the financial data that it used in performing the analytical procedures, in that its testing of the historical data was limited to inquiry;

- In its contract testing, failed to sufficiently test the issuer's contract costs, in that it failed to test the costs incurred to date, estimated costs to complete, and the completeness of the issuer's provision for loss contracts; and

- Failed to test the completeness of certain billing and sales reports that it used to test contract revenues.

20. Issuer T

In this audit, the Firm failed to obtain sufficient appropriate audit evidence to support its opinion on the issuer's ICFR. During the year under audit, the issuer made permanent a change it had recently made in the design of an important control it used to evaluate its securities for OTTI. As a result of this change, the issuer based the impairment evaluation for more of these securities than it had previously on summary security data rather than a more thorough analysis of the relevant circumstances regarding the unrealized losses. For the year under audit, the securities that were exempted from the requirement for a more thorough analysis had unrealized losses that aggregate to approximately eight times the Firm's established materiality level. The Firm failed to sufficiently evaluate the effect of this change on the design effectiveness of the control, as the Firm failed to obtain sufficient information about the modified control (*e.g.*, the severity, duration, or extent of unrealized losses for the securities for which more thorough analyses were no longer required) to determine whether the modified control operated with sufficient precision to prevent or detect misstatements that could be material to the financial statements.

21. Issuer U

In this audit, the Firm failed to sufficiently test the valuation of investments. Specifically, the Firm –

- Failed to obtain an understanding of the specific methods and assumptions underlying the fair value measurements obtained from pricing services and used in the Firm's testing of the fair value of the issuer's hard-to-value financial instruments; and

- Failed to test the valuation of certain investments included in the Firm's sample selection.

22. Issuer V

In this audit, the Firm failed to sufficiently test the allowance for loan losses. Specifically, the Firm failed to evaluate the reasonableness of certain of management's assumptions and to test certain inputs used in a number of complex models that the issuer had developed to calculate the allowance for loan losses. Further, the Firm failed to test the design and operation of certain key aspects of those models.

23. Issuer W

In this audit, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and on the effectiveness of the issuer's ICFR.

For the last three years, the Firm had excluded approximately 80 percent of the issuer's consolidated entities, frequently the same entities from year to year, from direct testing by the Firm, primarily on the basis that these locations were individually immaterial. Together, these entities were responsible for 32 percent of the issuer's net sales and assets. The Firm identified a pervasive risk of management override and a specific risk of the improper timing of revenue recognition for all locations.

The Firm determined that it could use the work of the issuer's internal audit ("IA") function with respect to testing application controls and process controls at certain of these locations, and that controls at other locations did not need to be tested. The Firm, however, failed to adequately assess the sufficiency of IA's procedures, and failed to adequately respond to the findings of these procedures, in the following respects:

- The Firm failed to perform any procedures beyond inquiry to update IA's tests of controls, which covered only some or all of the first half of the year, through the year end.
- The Firm failed to evaluate the effect the large number of control deficiencies that IA identified at the locations should have had on the Firm's risk assessments and related audit procedures. Several of the control deficiencies identified were in areas where the Firm had identified a higher risk of material misstatement.

In addition, the Firm failed to perform sufficient substantive procedures for those locations with respect to revenue and related costs, accounts receivable, and inventory. Specifically, in performing the analytical procedures that it used to test revenue for these locations (as well as locations at which the Firm performed testing), the Firm inappropriately relied on controls in establishing thresholds for investigation. In addition, the procedures were performed at the operating-segment level, which did not represent sufficient disaggregation to provide the Firm with the necessary level of assurance.

24. Issuer X

In this audit, the Firm failed to sufficiently test the valuation of certain deferred costs, in that it failed to test the completeness and/or accuracy of certain of the data contained in reports that the Firm used to perform substantive tests of, and tests of controls over, the valuation of those deferred costs.

25. Issuer Y

In this audit, the Firm failed to perform sufficient procedures to test the accounting and disclosures regarding the issuer's defined benefit pension and other post-retirement benefit plans, as it designed its procedures based on a level of reliance on internal control that was excessive. Specifically, the Firm failed to identify and test any controls over the valuation of the pension plan assets and the completeness and accuracy of the participant data used to determine the accumulated benefit obligation of the plans.

26. Issuer Z

The Firm audited the financial statements of a subsidiary of the issuer based on instructions from a foreign affiliated firm. The Firm failed to obtain sufficient appropriate audit evidence to fulfill the objectives of its role in the audit. Specifically –

- The Firm failed to obtain an understanding of the specific methods and assumptions underlying the fair value measurements obtained from third parties and used in the Firm's testing of the fair value of the subsidiary's hard-to-value financial instruments.

- The Firm failed to perform sufficient procedures to evaluate the appropriateness of the subsidiary's fair value disclosures. Specifically, the Firm failed to test controls over the subsidiary's process for identifying the level for the subsidiary's securities within the fair value hierarchy set forth in FASB ASC Topic 820, *Fair Value Measurements and Disclosures*. The Firm also failed to perform sufficient substantive procedures to test the subsidiary's classification of securities within that hierarchy, as it failed to obtain an understanding of whether the significant inputs used to value the securities were observable or unobservable.

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 five areas (1) management structure and processes, including the tone at the top; (2) practices for partner management, including allocation of partner resources and partner evaluation, compensation, admission, and disciplinary actions; (3) policies and procedures for considering and addressing the risks involved in accepting and retaining clients, including the application of the Firm's risk-rating system; (4) processes related to the Firm's use of audit work that the Firm's foreign affiliates perform on the foreign operations of the Firm's U.S. issuer audit clients; and (5) the Firm's processes for

monitoring audit performance, including processes for identifying and assessing indicators of deficiencies in audit performance, independence policies and procedures, and processes for responding to weaknesses in quality control. 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

PART II, PART III, APPENDIX A, AND APPENDIX B OF THIS REPORT ARE NONPUBLIC AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

APPENDIX C

THE INSPECTION PROCESS FOR ANNUALLY INSPECTED FIRMS

The inspection process is designed, and inspections are performed, to provide a basis for assessing the degree of compliance by a firm with applicable requirements related to auditing issuers. This appendix describes the inspection process for those annually inspected firms that have multiple practice offices and a national office structure. While this appendix describes the general inspection process applied in the 2010 inspections of these firms, the process was customized to each firm's inspection, bearing in mind the firm's structure, past inspection observations, observations during the course of the 2010 inspection, and other factors. Accordingly, procedures described in this Appendix, while generally applicable to annual inspections, may not have been applied, or may not have been applied fully, in the inspection of any individual firm, and additional procedures, not described in this appendix, may have been applied in the inspection of an individual firm.

The inspection process included reviews of aspects of selected issuer audits completed by the inspected firm. These reviews were intended both to identify deficiencies, if any, in those aspects of the audits and to determine whether those deficiencies indicated weaknesses or defects in the firm's system of quality control over audits. In addition, the inspection included reviews of policies and procedures related to certain quality control processes of the firm that could be expected to affect audit quality.

1. Review of Selected Audits

Inspections include reviews of aspects of selected audits of financial statements and ICFR. For each audit selected, the inspection team reviewed certain of the issuer's SEC filings. The inspection team selected certain aspects of the audits for review and inspected the engagement team's work papers and interviewed engagement personnel regarding those aspects. The inspection team also analyzed potential adjustments to the issuer's financial statements that were identified during the audit but not corrected. For certain selected engagements, the inspection team reviewed written communications between the firm and the issuer's audit committee and, for some engagements, the inspection team interviewed the chairperson of the issuer's audit committee.

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 was allowed the opportunity to provide a written response to the comment form.

2. Review of Firm Management and Monitoring Processes Related to Audit Quality Control

The inspection team's review of a firm's system of quality control was intended to provide a basis for assessing whether that system was appropriately designed and implemented to achieve the goal of conducting audits that are in compliance with applicable standards. This review included an evaluation of the firm's ability to respond effectively to indications of possible defects in its system of quality control.

a. Review of Management Structure and Processes, Including the Tone at the Top

Procedures in this area were designed to focus on (a) how the firm's management is structured and operates the firm's business, and the implications that the management structure and processes have on audit performance, and (b) whether actions and communications by the firm's leadership – the "tone at the top" – demonstrate a commitment to audit quality. The inspection team interviewed members of the firm's leadership to obtain an understanding of any significant changes in the firm's approach to, and processes for, its management, including the mechanisms, formal or informal, that assess, monitor, or affect audit performance. The inspection team also reviewed significant management reports and documents, as well as information regarding financial metrics and the budget and goal setting processes that the firm uses to plan for, and evaluate the success of, its business.

b. Review of Practices for Partner Management, Including Allocation of Partner Resources and Partner Evaluation, Compensation, Admission, and Disciplinary Actions

Procedures in this area were designed to focus on (a) whether the firm's processes related to partner evaluation, compensation, admission, 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; (b) the firm's processes for allocating its partner resources; and (c) the accountability and responsibilities of the different levels of firm management with respect to partner management. The inspection team interviewed members of the firm's management and also reviewed documentation related to certain of these topics. In addition, the inspection team's interviews of audit partners included questions regarding their responsibilities and allocation of time and the interviews of firm management included the performance of partners being inspected, the evaluation and compensation process, any disciplinary actions, and any situations where a client requested a change in the lead audit partner. In addition, the inspection team reviewed a sample of partners' personnel files, including files of partners who resigned or took early retirement

and partners who had significant negative inspection results from recent internal and PCAOB inspections.

c. Review of Policies and Procedures for Considering and Addressing the Risks Involved in Accepting and Retaining Clients, Including the Application of the Firm's Risk-Rating System

The inspection team selected certain issuer audits to (a) evaluate compliance with the firm's policies and procedures for identifying and assessing the risks involved in accepting or continuing the client and (b) observe whether the audit procedures were responsive to the risks identified during the process.

d. Review of Processes Related to the Firm's Use of Audit Work that the Firm's Foreign Affiliates Perform on the Foreign Operations of the Firm's U.S. Issuer Audit Clients

The inspection team reviewed the firm's policies and procedures related to its supervision and control of work performed by foreign affiliates on the operations of U.S. issuer clients, reviewed available information relating to the most recent foreign affiliated firms' internal inspections, interviewed members of the firm's leadership, and reviewed the U.S. engagement teams' supervision and control procedures concerning the audit work that the firm's foreign affiliates performed on a sample of audits. In some cases, the inspection team also reviewed, on a limited basis, certain of the audit work performed by the firm's foreign affiliates on the foreign operations of U.S. issuer clients.

e. Review of the Firm's Processes for Monitoring Audit Performance, Including Processes for Identifying and Assessing Indicators of Deficiencies in Audit Performance, Independence Policies and Procedures, and Processes for Responding to Weaknesses in Quality Control

(i) Review of Processes for Identifying and Assessing Indicators of Deficiencies in Audit Performance

Procedures in this area were designed to identify and assess the monitoring processes that the firm uses to monitor audit quality for individual engagements and for the firm as a whole. The inspection team interviewed members of the firm's management and reviewed documents regarding how the firm identifies, evaluates, and responds to possible indicators of deficiencies in audit performance, including internal inspection findings, PCAOB inspection observations, restatements, and litigation. In addition, the inspection team reviewed documents related to the design, operation, and evaluation of findings of the firm's internal inspection program. The inspection team

also reviewed certain audits that the firm had inspected and compared its results to those from the internal inspection.

(ii) Review of Response to Weaknesses in Quality Control

The inspection team reviewed steps the firm has taken in the past several years to address possible quality control deficiencies. The inspection team then assessed the design and evaluated the effectiveness of the processes identified. 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.

(iii) Review of Certain Other Policies and Procedures Related to Monitoring Audit Quality

The inspection team assessed policies, procedures, and guidance related to aspects of the firm's independence requirements and its consultation processes and the firm's compliance with them. In addition, the inspection team reviewed documents, including certain newly issued policies and procedures, and interviewed firm management to consider the firm's methods for developing audit policies, procedures, and methodologies, including internal guidance and training materials.

APPENDIX D

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.[9/]

[9/] 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.

Deloitte.

Deloitte & Touche LLP
1633 Broadway
New York, NY 10019
USA

November 21, 2011

Mr. Christopher D. Mandaleris
Senior Deputy Director
Division of Registration and Inspections
Public Company Accounting Oversight Board
1666 K Street NW
Washington, DC 20006

Re: Deloitte & Touche LLP – Response to Part I of Draft Report on 2010 Inspection

Dear Mr. Mandaleris:

Deloitte & Touche LLP is pleased to submit our response to the October 19, 2011, draft of Report on 2010 Inspection of Deloitte & Touche LLP (the Draft Report) of the Public Company Accounting Oversight Board (the PCAOB or the Board). We believe that the PCAOB's inspection process serves an important role in the achievement of our shared objectives of improving audit quality and serving investors and the public interest. We are committed to the highest standards of audit quality.

We have evaluated the matters identified by the Board's inspection team for each of the issuer audits described in Part I of the Draft Report and have taken actions as appropriate in accordance with PCAOB standards to comply with our professional responsibilities under 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.*

We are committed to continuing to work with the PCAOB to further strengthen trust in the integrity of the independent audit. We are available to the Board and its staff to discuss any aspect of our response or any further questions you may have.

Sincerely,

Deloitte & Touche LLP

cc:

James R. Doty, Chairman
Lewis H. Ferguson, Board Member
Daniel L. Goelzer, Board Member
Jay D. Hanson, Board Member
Steven B. Harris, Board Member
Helen A. Munter, Director
Paul E. Bijou, Deputy Director