

ORDER

Respondent consents to entry of this Order Instituting Disciplinary Proceedings, Making Findings and Imposing Sanctions ("Order") as set forth below.¹

III.

On the basis of Respondent's Offer, the Board finds that:

A. Respondent

1. PricewaterhouseCoopers LLP is a limited liability partnership organized under the laws of Delaware, and headquartered in New York, New York. PwC registered with the Board on October 20, 2003, pursuant to Section 102 of the Act and PCAOB rules. Since fiscal year ("FY") 2009, PwC has been the external auditor for Merrill.

B. Broker-Dealer²

2. At all relevant times, Merrill was a Delaware corporation headquartered in New York, New York. Merrill's public filings disclose that it is registered with the Commission as a broker-dealer and investment adviser, and is registered with the U.S. Commodity Futures Trading Commission as a futures commission merchant. Merrill is a wholly-owned indirect subsidiary of Bank of America Corporation. At all relevant times, Merrill was a "broker" and "dealer," as defined in Section 110(3) and (4) of the Act and PCAOB Rule 1001(b)(iii) and (d)(iii). Merrill is a "carrying broker-dealer" (i.e., a broker-dealer that maintains custody of customer funds and securities).

¹ The findings herein are made pursuant to Respondent's Offer and are not binding on any other persons or entities in this or any other proceeding.

² On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. L. No. 111-203, 124 Stat. 1376 (July 21, 2010)) amended various provisions of the Sarbanes-Oxley Act ("the Dodd-Frank amendments"). Among other things, the amendments provide the Board with authority to carry out the same oversight responsibilities it has carried out with respect to issuer audits – standards-setting, inspections, and investigations and disciplinary proceedings – in connection with registered public accounting firms' audits of brokers and dealers that are registered with the Commission.



ORDER

C. Summary

3. In 2014, Merrill held tens of billions of dollars of its customers' securities in certain accounts with third-party institutions that were subject to liens by the third parties,³ in violation of Commission Rule 15c3-3, 17 C.F.R. § 240.15c3-3, also known as the "Customer Protection Rule."⁴ Among other things, the Customer Protection Rule required broker-dealers like Merrill⁵ to hold certain customer securities in a segregated account free of liens (the "no-lien" requirement). The purpose of this requirement was to protect customer securities from claims by a failed broker-dealer's creditors. As Merrill's auditor, PwC was required to obtain sufficient appropriate evidence to support its opinion about (a) whether Merrill's internal controls over compliance with the Customer Protection Rule were effective during the period of June 1, 2014 to December 31, 2014 and at the end of FY 2014,⁶ and (b) whether supplemental information in certain filings by Merrill concerning its compliance with the Customer Protection Rule were fairly stated in all material respects, in relation to Merrill's financial statements as a whole. However, PwC failed to obtain sufficient evidence in each of these categories.

³ See *Merrill Lynch, Pierce, Fenner & Smith Inc. and Merrill Lynch Professional Clearing Corp.*, SEC Rel. No. 34-78141, at 3 (June 23, 2016).

⁴ Adopted in 1972, the "Customer Protection Rule" is Rule 15c3-3 issued by the Commission under the Securities Exchange Act of 1934 ("Exchange Act").

⁵ Although some broker-dealers qualify for exemption from the Customer Protection Rule, Merrill was a carrying broker-dealer and did not qualify for exemption under Rule 15c3-3(k).

⁶ During the transition period for the below-mentioned amendments to Exchange Act Rule 17a-5, 17 C.F.R. § 240.17a-5 ("Rule 17a-5"), the Commission's Division of Trading and Markets provided guidance that the staff will not object if a broker-dealer whose 2014 or 2015 fiscal year begins prior to June 1, 2014 submits statements in its compliance report that do not cover the period of the fiscal year that is prior to June 1, 2014. See Division of Trading and Markets of the U.S. Securities and Exchange Commission, *Frequently Asked Questions Concerning the July 30, 2013 Amendments to the Broker-Dealer Financial Reporting Rule* (April 4, 2014), Question/Answer No. 1, <https://www.sec.gov/divisions/marketreg/amendments-to-broker-dealer-reporting-rule-faq.htm>. Accordingly, Merrill's assertions in its compliance report for FY 2014 covered only the period from June 1, 2014 to December 31, 2014.



ORDER

4. As a result, PwC violated PCAOB rules and standards, including Attestation Standard No. 1, *Examination Engagements Regarding Compliance Reports of Brokers and Dealers* ("AT 1"), when performing its examination of the statements made by Merrill in its FY ended December 31, 2014 compliance report (the "Examination") prepared pursuant to Rule 17a-5. In particular, PwC failed to adequately test Merrill's key internal controls over compliance with the "no-lien" requirement of the Customer Protection Rule.

5. Additionally, PwC violated PCAOB rules and standards, including Auditing Standard No. 17, *Auditing Supplemental Information Accompanying Audited Financial Statements* ("AS 17"), in connection with its performance of audit procedures and opining on supplemental information accompanying the financial statements of Merrill for FY ended December 31, 2014 (the "Audit"). In particular, PwC failed to obtain sufficient appropriate audit evidence to support its conclusion on one of Merrill's supporting schedules relating to its compliance with the Customer Protection Rule.

6. On February 26, 2016, Merrill restated its FY 2014 compliance report to disclose a material weakness in its internal control over compliance related to maintenance of custodial accounts in designated good control locations. That same day, PwC revised its FY 2014 examination report to reflect that Merrill did not maintain effective internal control over compliance because this material weakness existed during the period June 1 to December 31, 2014, and as of December 31, 2014.

D. Respondent Violated PCAOB Attestation Standard No. 1 in its Examination of Merrill's 2014 Compliance Report

Certain Commission Reporting Requirements for Merrill

7. The Customer Protection Rule required Merrill to promptly obtain and thereafter maintain physical possession or control over its customers' fully-paid securities and excess margin securities.⁷ Under the control requirement described in Rule 15c3-3(c), control generally means that the broker-dealer must hold these securities in one of several locations specified in the Rule and that they be held free of liens or any other interest that could be exercised by a third-party to secure an obligation of the broker-dealer.

⁷ See 17 C.F.R. § 240.15c3-3(b). For a definition of "fully paid securities" and "excess margin securities," see Rule 15c3-3(a)(3), (5), 17 CFR 240.15c3-3(a) (3), (5).



ORDER

8. As applicable to Merrill, Rule 15c3-3(c) provided that, if Merrill held customers' fully-paid and excess margin securities at a U.S. Bank, those securities would be deemed to be in Merrill's control if, among other things, "the bank . . . *acknowledged in writing* that the securities in its custody or control are not subject to any right, charge, security interest, lien or claim of any kind in favor of the bank or any person claiming through the bank."⁸ The Commission imposed a similar "no-lien" requirement for customer fully-paid or excess margin securities that Merrill held at a foreign depository or foreign custodian bank.⁹ The "no-lien" requirement of Rule 15c3-3(c) was in effect when PwC began its work on the Merrill engagement in 2009, and it remains in effect today.

9. Effective June 1, 2014, amendments to Rule 17a-5 required Merrill to file with the Commission an annual report containing (a) a financial report that included financial statements and supporting schedules,¹⁰ (b) a compliance report concerning the effectiveness of Merrill's internal controls over compliance with, among other things, the "no-lien" requirement;¹¹ and (c) a report by a PCAOB-registered firm based on an examination of Merrill's financial and compliance reports.¹² The amendments to Rule 17a-5 also required that the auditor's examinations of the financial report and compliance report be performed in accordance with PCAOB standards.¹³

10. In the compliance report, Merrill had to make certain statements ("assertions") about its compliance with, among other things, the Customer Protection Rule, including that (a) Merrill's internal control over compliance¹⁴ was effective during

⁸ See 17 C.F.R. § 240.15c3-3(c)(5) (emphasis added). This Order uses the term "U.S. Bank" to mean a bank as defined in section (3)(a)(6) of the Exchange Act.

⁹ See Rule 15c3-3(c)(4); Exchange Act Release 34-10429, *Guidelines for Control Locations for Foreign Securities Pursuant to Subparagraphs (c)(4) and (c)(7) of Rule 15c3-3 Under the Securities Exchange Act of 1934* (Oct. 12, 1973).

¹⁰ See Rule 17a-5(d)(1)(i)(A), (d)(2).

¹¹ See Rule 17a-5(d)(1)(i)(B)(1), (d)(3).

¹² See Rule 17a-5(d)(1)(i)(C), (g).

¹³ See Rule 17a-5(g).

¹⁴ Rule 17a-5(d)(3)(ii) provides: "The term *Internal Control Over Compliance* means internal controls that have the objective of providing the broker or dealer with reasonable assurance that non-compliance with [Exchange Act Rules 15c3-1, 15c3-3,

ORDER

the most recent fiscal year; and (b) its internal control over compliance was effective as of the end of the most recent fiscal year.¹⁵

PCAOB Attestation Standard No. 1

11. In connection with the preparation or issuance of an examination report for a broker-dealer, PCAOB rules require that a registered public accounting firm and its associated persons comply with the Board's auditing and related professional practice standards, including attestation standards.¹⁶

12. AT 1 became effective for audits of fiscal years ending on or after June 1, 2014, and established requirements aligned with the auditor's responsibilities under the amended Rule 17a-5. AT 1 provides that, in performing an examination of the assertions made by a broker or dealer in a compliance report (an "examination engagement"), the auditor's objective is to express an opinion regarding whether the assertions made by the broker or dealer in the compliance report are fairly stated, in all material respects.¹⁷ AT 1 also provides that, to express such opinion, the auditor must plan and perform the examination engagement to obtain appropriate evidence that is sufficient to obtain reasonable assurance about whether, among other things, one or more material

17a-13], or any rule of the designated examining authority of the broker or dealer that requires account statements to be sent to the customers of the broker or dealer (an 'Account Statement Rule') will be prevented or detected on a timely basis."

¹⁵ See Rule 17a-5(d)(3)(i)(A).

¹⁶ See PCAOB Rule 3100, *Compliance with Auditing and Related Professional Practice Standards*, and PCAOB Rule 3200T, *Interim Auditing Standards*. All references to PCAOB standards are to the versions of those standards in effect at the time of the Merrill Audit. As of December 31, 2016, the PCAOB reorganized its auditing standards using a topical structure and a single, integrated numbering system. See *Reorganization of PCAOB Auditing Standards and Related Amendments to PCAOB Standards and Rules*, PCAOB Release No. 2015-002 (Mar. 31, 2015); see also *PCAOB Auditing Standards Reorganized and Pre-Reorganized Numbering* (January 2016), <https://pcaobus.org/Standards/Auditing/Documents/PrintableReferenceTable.pdf>.

¹⁷ See AT 1 ¶ 3.

ORDER

weaknesses¹⁸ existed during the most recent fiscal year being reported.¹⁹ As noted in AT 1, the auditor's examination should include an evaluation of the effectiveness of internal control over compliance with the Customer Protection Rule during, and as of the end of, the most recent fiscal year.²⁰

13. AT 1 also provides that the auditor must exercise due professional care, which includes application of professional skepticism, in planning and performing the examination engagement.²¹ Additionally, when planning the examination engagement, the auditor should obtain an understanding of the broker-dealer's processes regarding compliance with, among other things, the Customer Protection Rule, which includes evaluating the design of controls that are relevant to the examination and determining whether they have been implemented.²² When performing the examination engagement, the auditor must test the controls that are important to the auditor's conclusion about whether the broker-dealer has maintained effective internal control over compliance for, among other things, the Customer Protection Rule during the fiscal year and at fiscal year end, and must obtain evidence that the tested controls are designed effectively and operated effectively during the fiscal year and at fiscal year end.²³

14. If controls selected for testing in the current year were tested in past examination engagements, and if the auditor plans to use evidence about the effectiveness of those controls that was obtained in prior years, the auditor should take

¹⁸ A "material weakness" is a deficiency, or a combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that non-compliance to a material extent with Rule 15c3-3(c), among other things, will not be prevented or detected on a timely basis. See AT 1, Appendix A ¶ A4.

¹⁹ See AT 1 ¶ 4.

²⁰ See id. ¶ 4, Note.

²¹ See id. ¶ 6(d).

²² See id. ¶ 9(b) and Note.

²³ See id. ¶ 11. The auditor should test the design effectiveness of the selected controls by determining, among other things, whether the control can effectively prevent or detect instances of non-compliance with the Customer Protection Rule on a timely basis. See id. ¶ 14. Additionally, the auditor should test the operating effectiveness of the selected controls by determining whether each is operating as designed, among other things. See id. ¶ 16.

ORDER

into account numerous factors to determine the evidence needed during the current fiscal year examination, including (a) the nature, timing, and extent of procedures performed in previous examination engagements; (b) the results of the previous years' testing of the controls; and (c) any changes in the controls or the process in which the control operates since the previous examination engagement.²⁴ Additionally, when an auditor uses information produced by the company as audit evidence, the auditor should evaluate whether the information is sufficient and appropriate for purposes of the audit by performing procedures to test the accuracy and completeness of the information, or test the controls over the accuracy and completeness of that information.²⁵

15. As provided in AT 1, the auditor should evaluate whether he or she has obtained sufficient appropriate evidence to support the conclusions to be presented in the examination report, taking into account the risks associated with controls and non-compliance, the results of the examination procedures performed, and the appropriateness (*i.e.*, the relevance and reliability) of the evidence obtained.²⁶ If the auditor is unable to obtain sufficient appropriate evidence about an assertion, the auditor should express a disclaimer of opinion.²⁷

16. As described below, Respondent failed to comply with applicable PCAOB rules and standards in connection with its Examination of the assertions made by Merrill in its FY ended December 31, 2014 compliance report.

Respondent's Examination of Merrill's 2014 Compliance Report

17. On March 2, 2015, Merrill filed its Form X-17A-5 Part III for FY 2014 with the Commission. In connection with that filing, Merrill filed its FY 2014 compliance report dated February 27, 2015 ("Compliance Report"). The Compliance Report's assertions included that Merrill's internal control over compliance with the Customer Protection Rule was effective during the period from June 1, 2014 to December 31, 2014, and also as of

²⁴ See *id.* ¶ 19.

²⁵ See Auditing Standard No. 15, *Audit Evidence* ("AS 15"), ¶ 10.

²⁶ See AT 1 ¶ 27.

²⁷ See *id.* ¶ 29.



ORDER

December 31, 2014.²⁸ PwC issued its examination report, dated February 27, 2015, concerning Merrill's Compliance Report ("Examination Report"). PwC's Examination Report expressed its unqualified opinion that Merrill's assertions in the Compliance Report were fairly stated, in all material respects, and the Examination Report stated, among other things, that the Examination was conducted in accordance with PCAOB standards.

18. During the Examination, PwC was aware that Merrill maintained some of its customers' fully-paid securities and excess margin securities in Merrill's own physical possession, and held the rest – amounting to billions of dollars in customer securities – in accounts at various third-party institutions. PwC understood that Merrill designated all of these accounts as "good control locations" (*i.e.*, compliant with the Customer Protection Rule's requirements to keep customers' fully-paid securities and excess margin securities either in Merrill's possession, or in Merrill's control if the securities were held at a third-party institution). The third-party accounts were at different types of custodians, such as U.S. Banks and foreign depositories. All of the accounts at third-party institutions were governed by custodial agreements between Merrill and the institutions.

19. PwC was aware of the magnitude of customer fully-paid and excess margin securities that Merrill held in accounts at third-party institutions in 2014, and was aware of the risks to Merrill's customers if those accounts were subject to liens. Nevertheless, PwC failed to plan and perform its Examination to obtain sufficient evidence concerning Merrill's compliance with the "no-lien" requirement of the Customer Protection Rule. In particular, PwC failed to obtain an adequate understanding of Merrill's internal control over compliance with the "no-lien" requirement of the Customer Protection Rule.²⁹ Specifically, PwC failed to adequately test both the design effectiveness and operating effectiveness of the controls that were important to its conclusion about whether Merrill maintained effective internal control over compliance with the "no-lien" requirement of the Customer Protection Rule.³⁰ PwC therefore failed to obtain appropriate evidence sufficient to provide reasonable assurance about whether

²⁸ As noted above, Merrill's Compliance Report assertion about effectiveness of internal control over compliance during the most recent fiscal year only covered the period June 1, 2014 to December 31, 2014.

²⁹ See AT 1 ¶ 9(b) and Note.

³⁰ See *id.* ¶¶ 11, 14, 16.

ORDER

there were material weaknesses in Merrill's internal control over compliance, as required by AT 1.³¹

PwC's Inadequate Control Testing

20. During the Examination, PwC identified Merrill's key control relevant to its compliance with Rule 15c3-3(c) when designating accounts as good control locations (the "Key Control"). As explained below, in its Examination, PwC failed to obtain reasonable assurance about whether one or more material weaknesses existed in Merrill's internal control over compliance with Rule 15c3-3(c) during June – December 2014 and at year end 2014.

Inadequate Testing of Design Effectiveness

21. PwC performed a walkthrough of the Key Control to test its design effectiveness. The work paper documenting the walkthrough noted that Merrill produced a daily Production Report. The Production Report identified when Merrill had designated a new account as a good control location, or had changed the designation of an existing account to a good control location (collectively, "newly-designated" accounts). Although the walkthrough work paper stated that Merrill "reviews & validates" the custodial agreements for the newly-designated accounts appearing on the Production Report to determine whether Merrill properly designated them as good control locations, PwC did not obtain an understanding of what specific criteria the Key Control required Merrill to use in making such determinations. In fact, neither PwC's walkthrough procedures, nor any other testing of the Key Control, indicated whether Merrill considered the "no-lien" requirement of the Customer Protection Rule when designating good control locations. Consequently, PwC did not obtain sufficient appropriate evidence from the walkthrough that the Key Control was designed such that it could effectively prevent or detect instances of non-compliance with the Customer Protection Rule on a timely basis, as required by PCAOB standards.³²

Inadequate Testing of Operating Effectiveness

22. To test the operating effectiveness of the Key Control, PwC selected a sample of days during June – December 2014 and obtained and reviewed the Production Report for each day selected. These reports identified five newly-designated

³¹ See id. ¶ 4; Appendix A ¶ A4.

³² See AT 1 ¶¶ 11, 14.

ORDER

good control locations, two of which were accounts held at third-party institutions to which the "no-lien" requirement applied. PwC obtained from Merrill the custody agreements for these two accounts, and concluded that the Key Control operated effectively during June – December 2014 and at year end 2014.

23. However, this testing did not provide PwC with evidence that the Key Control operated effectively in 2014. First, the two custody agreements that PwC obtained for the third-party institutions did not contain evidence that the accounts were free of liens and other encumbrances, as required by Rule 15c3-3(c). Second, PwC did not obtain evidence that Merrill personnel actually "review[ed] & validate[d]" the account documents of good control locations, in accordance with the design of the Key Control. In fact, PwC's evidence of two custodial agreements without "no-lien" provisions should have raised questions as to whether Merrill custodial agreements complied with the "no-lien" requirements, and whether Merrill's personnel were adequately reviewing the custody agreements for "no-lien" provisions. As a result, PwC violated PCAOB standards by failing to obtain sufficient evidence that the Key Control operated effectively during June – December 2014 and at year end 2014.³³

Failure to Obtain Reasonable Assurance About Material Weaknesses in Internal Control Over Compliance

24. Even if PwC had obtained evidence that the Key Control was designed effectively and operated effectively during June – December 2014 and at year end 2014, that evidence would not have been sufficient to provide reasonable assurance about whether one or more material weaknesses existed in Merrill's internal control over compliance with Rule 15c3-3(c) in 2014.³⁴ By design, the Key Control was to operate in 2014 to address compliance only with respect to the good control locations that were newly-designated *in 2014*. Thus, for the rest of Merrill's good control locations that had been designated in previous years but still existed in 2014, as PwC knew, Merrill was relying on the premise that its internal controls had operated effectively in previous years to prevent or detect non-compliance with the "no-lien" requirement in those years.³⁵

³³ See *id.* ¶¶ 11, 16.

³⁴ See *id.* ¶¶ 3-4.

³⁵ For 2009 to 2013, PwC's testing for compliance with Rule 15c3-3(c) was performed under the standards in place before AT 1 became effective, and was different from its testing in 2014. In those previous years, PwC did not use a Merrill Production Report in its testing. Instead, PwC obtained from Merrill a list of all Merrill-designated

ORDER

25. Accordingly, approximately 32 newly-designated good control locations were subject to the Key Control in 2014, out of a total of approximately 775 existing "good control locations" at Merrill as of year end 2014. For the approximately 743 previously-designated good control locations still existing as of year end 2014, PwC used the results of its testing in previous years to conclude that Merrill's internal controls over compliance had operated effectively in the previous years when those accounts had been designated.³⁶ Those results, however, did not provide sufficient appropriate evidence of the effectiveness of Merrill's internal control over compliance with the "no-lien" requirement for those previous years.

Merrill-designated Good Control Locations	
All existing accounts designated as good control locations by Merrill as of YE 2014	775
All accounts newly-designated as good control locations by Merrill in 2014	32
Newly-designated good control locations selected for FY 2014 testing by PwC	5

26. For example, in its testing for each of the previous years, PwC never obtained any evidence, such as custodial agreements with "no-lien" provisions, that accounts at U.S. Banks that Merrill had designated as good control locations satisfied

good control locations as of the end of the year under audit and compared that list to a list of all Merrill-designated good control locations as of the end of the prior year. PwC then identified which accounts were newly-designated in the year under audit, and selected test sample items from that group of accounts. PwC used the information in those Merrill-produced lists as audit evidence, but never performed sufficient procedures to test the accuracy and completeness of that information, or test the controls over the accuracy and completeness of that information. Consequently, under PCAOB standards, PwC could not use that information as audit evidence for the 2014 Examination and Audit. See AS 15 ¶ 10.

³⁶ For FY 2014, PwC could not rely on evidence obtained in its previous years' control testing without taking into account the results of that testing. See AT 1 ¶ 19.



ORDER

the "no-lien" requirement of Rule 15c3-3(c). Even though PwC selected such accounts as sample items in its testing for each of the previous years, it failed to obtain evidence that Merrill personnel had validated that the accounts were protected by "no-lien" provisions.

27. Additionally, with respect to foreign depositories that Merrill had designated as good control locations, PwC selected certain accounts from those depositories for testing in prior years, but failed to consistently obtain sufficient evidence that the accounts selected satisfied the "no-lien" requirement of Rule 15c3-3(c), and failed to obtain evidence that Merrill personnel had validated that the selected accounts were protected by "no-lien" provisions.

28. Consequently, for purposes of compliance with the "no-lien" requirement, PwC failed to obtain sufficient appropriate evidence that Merrill's internal controls had operated effectively with respect to the previously-designated good control locations still existing in 2014.

29. As noted above, from 2009 to 2014, Merrill exposed tens of billions of dollars of its customers' fully-paid securities and excess margin securities to potential liens by some of the third-party institutions at which Merrill had held those assets. Merrill held a majority of those exposed securities in one of the U.S. Bank accounts that it erroneously designated as a good control location – the account had market values ranging from about \$60 billion at year end 2009 to about \$30 billion at year end 2014.³⁷ With respect to certain third-party foreign depositories that Merrill had designated as good control locations, at year end 2014, billions of dollars in customers' securities were held in six accounts subject to a lien, and in 48 more accounts for which Merrill could not locate contemporaneous documentation establishing that the accounts satisfied the "no-lien" requirement of Rule 15c3-3(c). The deficiencies in Merrill's internal control over compliance that failed to prevent or detect the existence of such liens created a reasonable possibility of Merrill's non-compliance to a material extent with the Customer Protection Rule – i.e., a material weakness.³⁸

³⁷ This account did not comply with Rule 15c3-3(c) because the account was subject to a general lien by the U.S. Bank.

³⁸ See AT 1, Appendix A, ¶ A4.

ORDER

30. As a result of the above deficiencies, Respondent lacked a reasonable basis for its opinion that Merrill's assertions in its 2014 Compliance Report were fairly stated, in all material respects. Therefore, Respondent violated AT 1.³⁹

E. Respondent Violated PCAOB Rules and Standards in Its Audit of One of Merrill's 2014 Supporting Schedules

31. Rule 17a-5 required that Merrill file certain supplemental information in supporting schedules accompanying its 2014 financial statements, and that the schedules be audited by a PCAOB-registered firm.⁴⁰

32. In connection with the preparation or issuance of an audit report on such supplemental information, PCAOB rules require that a registered public accounting firm and its associated persons comply with the Board's auditing and related professional practice standards.⁴¹ Among other things, PCAOB standards require an auditor to exercise due professional care and professional skepticism in performing the audit.⁴²

33. PCAOB standards also require that, when the auditor is engaged to audit supplemental information accompanying the financial statements, the auditor should perform audit procedures to obtain appropriate audit evidence sufficient to support the auditor's opinion regarding whether the supplemental information is fairly stated, in all material respects, in relation to the financial statements as a whole.⁴³ In doing so, the auditor should, among other things, obtain an understanding of the criteria that management used to prepare the supplemental information, including relevant regulatory requirements.⁴⁴ The auditor also should perform procedures to test the completeness and accuracy of the information presented in the supplemental information, and should

³⁹ See *id.* ¶¶ 3-4.

⁴⁰ See Rule 17a-5(d)(1)(i)(A), (d)(1)(i)(C), (d)(2), and (g).

⁴¹ See PCAOB Rule 3100 and PCAOB Rule 3200T.

⁴² See AU § 150, *Generally Accepted Auditing Standards*; AU § 230, *Due Professional Care in the Performance of Work*.

⁴³ See AS 17 ¶¶ 2-3.

⁴⁴ See *id.* ¶ 4(a).

ORDER

evaluate whether the supplemental information complies with relevant regulatory requirements.⁴⁵

34. According to PCAOB standards, if an auditor is unable to obtain sufficient appropriate audit evidence to support an opinion on the supplemental information, the auditor should disclaim an opinion on the supplemental information.⁴⁶

35. As described below, Respondent failed to comply with PCAOB rules and standards in connection with the audit procedures it performed on the supplemental information in a supporting schedule accompanying Merrill's 2014 financial statements.

*Inadequate Audit Procedures on Supplemental Information
in Merrill's Supporting Schedule*

36. On March 2, 2015, Merrill filed Form X-17A-5 Part III for FY 2014 with the Commission. Included in that filing was PwC's FY 2014 audit report dated February 27, 2015. The audit report expressed an unqualified opinion on Merrill's financial statements and accompanying supporting schedules, and stated that PwC's audit was conducted in accordance with PCAOB standards. The audit report also stated that the supplemental information in an accompanying supporting schedule – Schedule IV, *Unconsolidated Information Relating to the Possession or Control Requirements for Brokers and Dealers Pursuant to Rule 15c3-3 under the Securities and Exchange Act of 1934* – was subjected to audit procedures in connection with PwC's audit of Merrill's financial statements. In particular, PwC represented that it had performed procedures to test the completeness and accuracy of the information presented in the supplemental information.⁴⁷

37. Rule 17a-5 required Merrill to file the Schedule IV to report on issues relating to Merrill's compliance with the possession or control requirements of the

⁴⁵ See *id.* ¶ 4(e) – (f).

⁴⁶ See *id.* ¶ 15.

⁴⁷ According to PCAOB standards, "[t]he auditor should take into account relevant evidence from . . . the attestation engagement[] . . . in planning and performing audit procedures related to the supplemental information and in evaluating the results of the audit procedures to form an opinion on the supplemental information." AS 17 ¶ 3(c), Note.



ORDER

Customer Protection Rule.⁴⁸ Merrill's Schedule IV as of December 31, 2014 reported, among other things, that there were no "[c]ustomers' fully paid securities and excess margin securities for which instructions to reduce to possession or control had not been issued as of the report date, excluding items arising from temporary lags . . . , as permitted under Rule 15c3-3." In part, Merrill's supplemental information represented that, with respect to customers' fully paid and excess margin securities that it held in accounts at U.S. Banks and foreign depositories, Merrill had issued instructions (whether through custodial agreements or otherwise) to maintain the securities in compliance with the "no-lien" requirement. PwC opined in its audit report that the Schedule IV was fairly stated, in all material respects, in relation to Merrill's financial statements as a whole.

38. But PwC had not obtained sufficient appropriate audit evidence to support its opinion. The only procedures that PwC performed relating to Merrill's compliance with the "no-lien" requirement were the above-mentioned testing of the Key Control and of the previous years' compliance with Rule 15c3-3(c). As described above, this testing was deficient, and PwC failed to obtain sufficient appropriate evidence of compliance with the "no-lien" requirement with respect to the Merrill-designated good control locations existing at year end 2014. PwC consequently failed to perform appropriate procedures to test the completeness and accuracy of the supplemental information presented in Merrill's Schedule IV for 2014, and failed to adequately evaluate whether that supplemental information complied with relevant regulatory requirements in Rule 15c3-3(c).⁴⁹

39. Respondent therefore violated PCAOB standards by failing to obtain sufficient appropriate audit evidence that the supplemental information in Merrill's supporting Schedule IV was fairly stated, in all material respects, in relation to the financial statements as a whole.⁵⁰

IV.

In view of the foregoing, and to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports, the Board determines it appropriate to impose the sanctions agreed to in Respondent's Offer. Accordingly, it is hereby ORDERED that:

⁴⁸ See Rule 17a-5(d)(1)(i)(A), (d)(2)(ii).

⁴⁹ See AS 17 ¶ 4(e) – (f).

⁵⁰ See *id.* ¶¶ 2-4.

ORDER

- A. Pursuant to Section 105(c)(4)(E) of the Act and PCAOB Rule 5300(a)(5), PricewaterhouseCoopers LLP is hereby censured; and
- B. Pursuant to Section 105(c)(4)(D) of the Act and PCAOB Rule 5300(a)(4), a civil money penalty in the amount of \$1,000,000 is imposed upon PricewaterhouseCoopers LLP. All funds collected by the Board as a result of the assessment of this civil money penalty will be used in accordance with Section 109(c)(2) of the Act. PricewaterhouseCoopers LLP shall pay the civil money penalty within 10 days of the issuance of this Order by (1) wire transfer in accordance with instructions furnished by Board staff; or (2) United States Postal Service money order, bank money order, certified check, or bank cashier's check (a) made payable to the Public Company Accounting Oversight Board, (b) delivered to the Controller, Public Company Accounting Oversight Board, 1666 K Street, N.W., Washington D.C. 20006, and (c) submitted under a cover letter, which identifies the payor as a respondent in these proceedings, sets forth the title and PCAOB release number of these proceedings, and states that payment is made pursuant to this Order, a copy of which cover letter and money order or check shall be sent to Office of the Secretary, Attention: Phoebe W. Brown, Secretary, Public Company Accounting Oversight Board, 1666 K Street, N.W., Washington D.C. 20006.

ISSUED BY THE BOARD.

/s/ Phoebe W. Brown

Phoebe W. Brown
Secretary

August 2, 2017