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ORDER INSTITUTING DISCIPLINARY
PROCEEDINGS, MAKING FINDINGS,
AND IMPOSING SANCTIONS

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)
) PCAOB Release No. 105-2015-002
)

) January 15, 2015
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In the Matter of Madsen & Associates
CPAs, Inc., and Ted A. Madsen, CPA,

Respondents.

By this Order, the Public Company Accounting Oversight Board ("Board" or "PCAOB") is censuring Madsen & Associates CPAs, Inc. ("Firm"), a registered public accounting firm, and revoking the Firm's registration;¹ and censuring Ted A. Madsen, CPA ("Madsen") and barring him from being an associated person of a registered public accounting firm.² The Board is imposing these sanctions on the basis of its findings that the Firm and/or Madsen (collectively, "Respondents") repeatedly violated PCAOB rules, auditing standards and quality control standards, violated Section 10A(a) of the Securities Exchange Act of 1934, and failed to timely disclose certain reportable events to the Board on PCAOB Form 3.

I.

The Board deems it necessary and appropriate, for the protection of investors and to further the public interest in the preparation of informative, accurate, and independent audit reports, that disciplinary proceedings be, and hereby are, instituted pursuant to Section 105(c) of the Sarbanes-Oxley Act of 2002, as amended (the "Act"), and PCAOB Rule 5200(a)(1) against Respondents.

¹ The Firm may reapply for registration after two (2) years from the date of this Order.

² Madsen may file a petition for Board consent to associate with a registered public accounting firm after two (2) years from the date of this Order.

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II.

In anticipation of institution of these proceedings, and pursuant to PCAOB Rule 5205, Respondents have each submitted an Offer of Settlement ("Offers") that the Board has determined to accept. Solely for purposes of these proceedings and any other proceedings brought by or on behalf of the Board, or to which the Board is a party, and without admitting or denying the findings herein, except as to the Board's jurisdiction over Respondents and the subject matter of these proceedings, which is admitted, Respondents consent to entry of this Order Instituting Disciplinary Proceedings, Making Findings, and Imposing Sanctions ("Order") as set forth below.³

III.

On the basis of Respondents' Offers, the Board finds⁴ that:

A. Respondents

1. Madsen & Associates CPAs, Inc. is, and at all relevant times was, a corporation organized under Utah law, and headquartered in Salt Lake City, Utah. The Firm is registered with the Board pursuant to Section 102 of the Act and PCAOB rules, and is licensed by the Utah Board of Accountancy (license no. 956535-2603). At all relevant times, the Firm was the external auditor for each of the issuers identified below.

2. Ted A. Madsen, CPA, age 60, is, and at all relevant times was, a certified public accountant licensed by the Utah Board of Accountancy (license no. 132743-2601). At all relevant times, Madsen owned a controlling interest in the Firm and was the Firm's quality control partner. Madsen is, and at all relevant times was, an associated person of a registered public accounting firm as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(i).

³ The findings herein are made pursuant to the Respondents' Offers and are not binding on any other person or entity in this or any other proceeding.

⁴ The sanctions that the Board is imposing on Respondents in this Order may be imposed only if a respondent's conduct meets one of the conditions set out in Section 105(c)(5) of the Act, 15 U.S.C. § 7215(c)(5). The Board finds that each Respondent's conduct described in this Order meets the conditions set out in Section 105(c)(5), which provides that certain sanctions may be imposed in the event of: (A) intentional or knowing conduct, including reckless conduct, that results in a violation of the applicable statutory, regulatory, or professional standard; or (B) repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standard.



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B. Summary

3. This matter concerns Respondents' failures to comply with PCAOB rules and auditing standards in connection with the audit of the financial statements of Sino Agro Food, Inc. ("Sino Agro") for the year ended December 31, 2011, and the audit of the financial statements of REDtone Asia, Inc. ("REDtone") for the year ended May 31, 2011.

4. In the case of each audit, Respondents hired Hong Kong-based engagement team members who performed most of the audit work. Madsen violated PCAOB standards by failing to properly supervise the work of those engagement team members and to review their work to determine its proper performance.

5. Despite identifying possible manipulation of revenue as "[a] high priority" for the Sino Agro audit, Respondents failed to identify and assess, or failed to ensure that the engagement team had identified and assessed, the risks of material misstatement of revenue at the assertion level as required by PCAOB standards. Moreover, with respect to three long-term contracts that Sino Agro accounted for using the percentage-of-completion method and that generated thirty percent of the issuer's annual revenue, Respondents and the engagement team failed to assess the reasonableness of the estimates underlying management's percentage-of-completion calculations, and failed to audit total costs incurred and management's estimates of total costs to completion. Further, despite evidence in the work papers suggesting related-party transactions not disclosed in Sino Agro's financial statements, Respondents and the engagement team failed to perform adequate procedures to identify and test the valuation of related-party transactions and to test whether Sino Agro's related-party disclosures were complete and accurate. Respondents and the engagement team also failed to consider whether a possible undisclosed transaction between Sino Agro and its chief executive officer constituted an illegal act, and as a result, Respondents violated Section 10A(a) of the Securities Exchange Act of 1934 ("Exchange Act") by failing to include audit procedures designed to provide reasonable assurance of detecting illegal acts that would have a direct and material effect on the financial statements.

6. Despite identifying overstatement of revenue as an audit and fraud risk for the REDtone audit, Respondents failed to perform, or failed to ensure that the engagement team had performed, audit procedures sufficient to provide reasonable assurance that the issuer's reported revenues were fairly stated. Moreover, Respondents and the engagement team failed entirely to test REDtone's reported accounts receivable balance.

7. The Firm also failed to comply with PCAOB quality control standards in connection with both audits, and Madsen took or omitted to take actions knowing, or

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recklessly not knowing, that his acts and omissions would directly and substantially contribute to the Firm's violations of PCAOB quality control standards. Finally, the Firm failed timely to disclose certain reportable events to the Board on Form 3 as required by PCAOB rules.

C. Respondents Violated PCAOB Rules and Auditing Standards

8. In connection with the preparation or issuance of an audit report, PCAOB rules require that a registered public accounting firm and its associated persons comply with the Board's auditing and related professional practice standards.⁵ An auditor may express an unqualified opinion on an issuer's financial statements only when the auditor has formed such an opinion on the basis of an audit performed in accordance with PCAOB standards.⁶

9. For audits of fiscal years ("FY") beginning before December 15, 2010, those standards require, among other things, that the auditor obtain sufficient competent evidence to afford a reasonable basis for an opinion regarding the financial statements,⁷ and that the efforts of assistants who perform work on the audit are properly supervised and that their work is reviewed to determine that it was adequately performed.⁸ For audits of fiscal years beginning on or after December 15, 2010, those standards require, among other things, that the auditor plan and perform the audit to obtain appropriate audit evidence that is sufficient to support the opinion expressed in the auditor's report;⁹ those standards also make the engagement partner responsible for proper supervision of engagement team members, including that their work be reviewed to evaluate whether it was properly performed and documented.¹⁰

⁵ PCAOB Rule 3100, *Compliance with Auditing and Related Professional Practice Standards*, and PCAOB Rule 3200T, *Interim Auditing Standards*. This Order applies PCAOB auditing standards in effect at the time of the conduct described herein.

⁶ See AU § 508.07, Reports on Audited Financial Statements.

⁷ See AU § 326, *Evidential Matter*.

⁸ See AU §§ 311.01 and 311.11-.14, *Planning and Supervision*.

⁹ See Auditing Standard No. 15, *Audit Evidence* ("A.S. 15").

¹⁰ See Auditing Standard No. 10, *Supervision of the Audit Engagement* ("A.S. 10").

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10. PCAOB standards further require that an auditor exercise due professional care and professional skepticism in performing the audit.¹¹ In addition, PCAOB standards require the auditor to obtain satisfaction concerning the purpose, nature, and extent of related party transactions through the performance of certain procedures that extend beyond management inquiry.¹² Those standards also require the auditor to evaluate the information available concerning related party transactions in order to satisfy the auditor that they have been adequately disclosed in the financial statements.¹³ PCAOB standards also require the auditor to obtain and evaluate sufficient appropriate evidential matter to support significant accounting estimates, and to evaluate the reasonableness of accounting estimates made by management.¹⁴ Moreover, PCAOB standards require the auditor to identify and assess the risks of material misstatement at both the financial statement level and the assertion level.¹⁵

Audit of Sino Agro's FY 2011 Financial Statements

11. At all relevant times, Sino Agro was a Nevada corporation with its principal executive offices in Guangzhou, People's Republic of China ("PRC"). Sino Agro's public filings disclosed that it was an integrated developer, producer and distributor of organic food and agricultural products in the PRC.¹⁶ At all relevant times, Sino Agro's common stock was registered under Section 12(g) of the Exchange Act and was quoted on the Pink OTC Markets.¹⁷ At all relevant times, Sino Agro was an issuer as that term is defined by Section 2(a)(7) of the Act and PCAOB Rule 1001(i)(iii).

12. On April 10, 2012, Madsen, as the engagement partner, authorized the Firm's issuance of an audit report expressing an unqualified opinion on Sino Agro's financial statements for the year ended December 31, 2011. The report was included in

¹¹ See AU § 150.02, Generally Accepted Auditing Standards; AU § 230, Due Professional Care in the Performance of Work.

¹² See AU § 334.09, *Related Parties*.

¹³ *Id.* at § 334.11.

¹⁴ See AU § 342, Auditing Accounting Estimates.

¹⁵ See Auditing Standard No. 12, Identifying and Assessing Risks of Material Misstatement ("A.S. 12"), at ¶ 59.

¹⁶ Sino Agro Food, Inc., Form 10-K for the year ended December 31, 2011 (April 12, 2012).

¹⁷ Since January 5, 2012, Sino Agro's common stock has been quoted on the OTC Bulletin Board.



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Sino Agro's Form 10-K filed with the Securities and Exchange Commission ("Commission" or "SEC") on April 12, 2012.

13. As the engagement partner on the FY 2011 Sino Agro audit, Madsen was responsible for the engagement and its performance, including compliance with PCAOB standards.¹⁸ Respondents hired Hong Kong-based engagement team members to perform most of the audit procedures. Madsen was responsible for properly supervising the work of those engagement team members, including reviewing their work to evaluate whether it was performed and documented; whether the objectives of the procedures were achieved; and whether the results of the work supported the conclusions reached.¹⁹ Madsen failed to properly supervise the work of engagement team members who performed procedures in the audit areas discussed below, and failed properly to review that work.

14. The work papers documented that "revenue recognition and manipulation of revenue/expenses is [a] high priority for [the] audit," but Respondents failed to identify and assess, or failed to ensure that the engagement team had identified and assessed, the risks of material misstatement of revenue at the assertion level as required by A.S. 12. Sino Agro reported total consolidated revenue of \$51.8 million in 2011, thirty percent of which (\$15.8 million) was generated from three long-term contracts entered into that year to provide consulting and construction services to related joint party ventures in connection with the construction of fish farms and hatcheries.²⁰ Sino Agro disclosed that revenues from these and other long-term contracts were accounted for under the percentage-of-completion method, in accordance with Financial Accounting Standards Board Accounting Standards Codification Topic 605, *Revenue Recognition*.²¹ Sino Agro's disclosures explained that under the percentage-of-completion method, "[t]he percentage of costs incurred determines the amount of revenue to be recognized... For fixed-price contracts, the Company uses the ratio of costs incurred to date on the contract ... to management's estimate of the contract's total costs, to determine the percentage of completion on each contract."²²

¹⁸ See A.S. 10, at ¶ 3.

¹⁹ *Id.*, at ¶ 5.

²⁰ Sino Agro Food, Inc., Form 10-K for the year ended December 31, 2011 (filed April 12, 2012).

²¹ *Id.*

²² *Id.*



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15. Respondents failed to obtain, or failed to ensure that the engagement team had obtained, sufficient audit evidence regarding the reasonableness of the estimates underlying management's percentage-of-completion calculations.²³ Further, the engagement team failed to audit the total costs incurred to date (through December 31, 2011) on the contracts, or Sino Agro's estimates of the total costs to completion.

16. Respondents failed to perform, or failed to ensure that the engagement team had performed, adequate procedures to determine the existence of related parties, to identify related-party transactions, and to test the valuation of identified related-party transactions. Moreover, Respondents failed to perform, or failed to ensure that the engagement team had performed, procedures to determine whether all significant related-party transactions and balances had been properly disclosed in Sino Agro's financial statements, and whether Sino Agro's related-party disclosures were complete and accurate.²⁴ Indeed, a management-prepared schedule in the work papers indicated that Sino Agro and a related party had entered into a prawn hatchery and nursery contract valued at \$8.08 million. That contract was not disclosed in Sino Agro's public filings, and there is no explanation in the work papers of why such disclosure was not made.

17. Other information in the work papers also conflicts with Sino Agro's related-party disclosures in the footnotes to its financial statements. Specifically, the work papers reflected that at the end of 2011, Sino Agro's chairman and chief executive officer owed an "other receivable" in the amount of ¥2.48 million (or approximately \$350,000) to a Sino Agro subsidiary. The work papers provided no explanation of why that amount due from the chairman and chief executive officer was not disclosed in the notes to Sino Agro's financial statements, even though a lesser amount due from him was disclosed. Finally, Respondents failed to consider, or failed to ensure that the engagement team had considered, whether the undisclosed transaction between Sino Agro and its chairman and chief executive officer might constitute an illegal act. As a result, Respondents violated Section 10A(a) of the Exchange Act by failing to include in the audit, procedures designed to provide reasonable assurance of detecting illegal

²³ See AU § 342.

²⁴ Section 10A of the Exchange Act requires that "each audit ... of the financial statements of an issuer by a registered public accounting firm shall include, in accordance with generally accepted auditing standards, as may be modified or supplemented from time to time by the Commission— [] (2) procedures designed to identify related party transactions that are material to the financial statements or otherwise require disclosure therein..."

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acts that would have a direct and material effect on the determination of financial statement amounts.²⁵

Audit of REDtone's FY 2011 Financial Statements

18. At all relevant times, REDtone was a Nevada corporation with its principal executive offices in Hong Kong. REDtone's public filings disclosed that it was in "the business of offering discounted call services...and paperless reload services for prepaid mobile air-time reload for end users in Shanghai [PRC] covering all three major telecommunications operators, namely China Mobile, China Unicom, and China Telecom," each of which was a PRC state-run entity.²⁶ At all relevant times, REDtone's common stock was registered under Section 12(g) of the Exchange Act and was quoted on the OTC Bulletin Board. At all relevant times, REDtone was an issuer as that term is defined by Section 2(a)(7) of the Act and PCAOB Rule 1001(i)(iii).

19. On August 26, 2011, Madsen, as the engagement partner, authorized the Firm's issuance of an audit report expressing an unqualified opinion on REDtone's financial statements for the year ended May 31, 2011. The report was included in REDtone's Form 10-K/A filed with the Commission on October 28, 2011.²⁷

20. Respondents hired Hong Kong-based assistants to perform most of the audit procedures. Madsen was the auditor with final responsibility for the FY 2011 REDtone audit and supervised the work of those assistants. Madsen failed to properly supervise the work of assistants who performed procedures in the audit areas discussed below, and failed to review that work to ensure that it was adequately performed.²⁸

21. In FY 2011, REDtone reported total consolidated revenue of \$5.4 million, 84% of which was generated by two subsidiaries that marketed and distributed call services in the PRC through arrangements with state-run telecommunication entities.²⁹

²⁵ See 15 U.S.C. § 78j-1(a)(1).

²⁶ REDtone Asia, Inc., Form 10-K/A for the year ended May 31, 2011 (October 28, 2011).

²⁷ In its Form 10-K/A filed on October 28, 2011, REDtone indicated that the Firm's audit report was inadvertently omitted from REDtone's Form 10-K for the year ended May 31, 2011, which was filed with the Commission on August 31, 2011.

²⁸ See AU §§ 311, at ¶¶ .01 and .11-.14.

²⁹ REDtone Asia, Inc., Form 10-K/A for the year ended May 31, 2011 (October 28, 2011).

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Respondents and the engagement team identified overstatement of revenue as an audit and fraud risk. Respondents failed to perform, or failed to ensure that the engagement team had performed, audit procedures sufficient to provide reasonable assurance that REDtone's FY 2011 revenues were fairly stated. The only procedures performed by the engagement team were walk-throughs of a single telephone call transaction for two subsidiaries and, for a small sample of transactions involving the same subsidiaries, a comparison of revenue amounts recorded in REDtone's general ledger with amounts reflected in sales reports generated by REDtone's information system. Regarding the latter testing, there was no evidence that test selections were made from a complete population of sales transactions. This limited testing failed to address the occurrence of REDtone's revenues and addressed accuracy only to the extent that REDtone's general ledger postings agreed to its own internal sales records.

22. In 2011, REDtone reported accounts receivable totaling \$645,000 (or approximately 5% of the company's total assets of \$12.6 million),³⁰ which were material to REDtone's FY 2011 financial statements. Because REDtone's receivable balance consisted primarily of receivables from two state-run entities, Respondents and the engagement team concluded that confirmation testing would be ineffective. While the audit plan included alternative procedures to test the receivable balance by tracing receivables to subsequent cash receipts, no such testing or any other testing of accounts receivable was performed.

D. The Firm Violated PCAOB Rules and Quality Control Standards And Madsen Contributed to Those Violations

23. PCAOB rules require that a registered public accounting firm comply with the Board's quality control standards,³¹ which, in turn, require that a registered public accounting firm "shall have a system of quality control for its accounting and auditing practice."³² Under PCAOB quality control standards, a firm should establish policies and procedures that "provide the firm with reasonable assurance that the work performed by engagement personnel meets applicable professional standards, regulatory requirements, and the firm's standards of quality."³³ The standards also provide that policies and procedures "should be established to provide the firm with

³⁰ Id.

³¹ PCAOB Rule 3100 and PCAOB Rule 3400T, *Interim Quality Control Standards*.

³² See QC § 20.02, System of Quality Control for a CPA Firm's Accounting and Auditing Practice.

³³ See QC § 20.17.



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reasonable assurance that the policies and procedures established by the firm for each of the other elements of quality control . . . are suitably designed and are being effectively applied," and that "its system of quality control is effective."³⁴ Those procedures should encompass "all phases of the design and execution of the engagement," including "planning, performing, supervising, reviewing, documenting, and communicating the results of each engagement."³⁵

24. The Firm failed to comply with these PCAOB quality control standards in connection with the FY 2011 Sino Agro and REDtone audits. Specifically, at all relevant times, the Firm failed to put in place policies and procedures to ensure that engagement personnel performed the audit procedures necessary to comply with all PCAOB auditing standards. As a result, in multiple instances, engagement personnel failed to complete necessary audit work before the Firm released its audit opinions for the FY 2011 Sino Agro and REDtone audits.

25. As evidenced by the multiple audit violations in each of the audits discussed above, the Firm's system of quality controls and quality control procedures did not provide the Firm with reasonable assurance that the work performed by engagement personnel met applicable professional standards, regulatory requirements, and the Firm's standards of quality, and did not provide the Firm with reasonable assurance that the policies and procedures established by the Firm were effectively applied.

26. PCAOB Rule 3502 prohibits an associated person of a registered public accounting firm from taking or omitting to take an action knowing, or recklessly not knowing, that the act or omission would directly and substantially contribute to a violation of Board standards by that firm.³⁶ Madsen, the managing member of the Firm, was principally responsible for designing, implementing, and monitoring the Firm's system of quality control. Accordingly, Madsen had overall responsibility for ensuring that the Firm complied with PCAOB rules and standards. All of the Firm's conduct described above constitutes acts or omissions to act by Madsen for which he was responsible. Madsen knew, or was reckless in not knowing, that his acts and omissions would directly and substantially contribute to the Firm's quality control violations described above. As a result, he violated PCAOB Rule 3502.

³⁴ See QC § 20.20; see also QC § 30.03, Monitoring a CPA Firm's Accounting and Auditing Practice.

³⁵ See QC § 20.18.

³⁶ PCAOB Rule 3502, Responsibility Not to Knowingly or Recklessly Contribute to Violations.

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E. The Firm Failed to Timely Disclose Certain Reportable Events to the Board

27. Promulgated pursuant to Section 102(d) of the Act, PCAOB Rule 2203 provides that a registered public accounting firm must file a special report on Form 3 to report any event specified in that form within thirty days of the event's occurrence.³⁷

28. By December 31, 2009, Madsen was aware that the Commission had sued L. Rex Andersen, CPA ("Andersen"), who then was partner of the Firm performing issuer audits, in a civil fraud action in federal district court relating to his work concerning an issuer audit that predated his association with the Firm.³⁸ On or about May 17, 2010, Madsen became aware, from reading a Commission release, that a final judgment and permanent injunction had been entered against Andersen in the aforementioned civil action.³⁹ On or about June 10, 2010, Madsen became aware, again from reading a Commission release, that Andersen had been named a respondent in public administrative proceedings pursuant to Rule 102(e)(3) of the Commission's Rules of Practice.⁴⁰ Although each of those three events constituted a reportable event, the Firm failed to file Forms 3 reporting the events to the Board.⁴¹

29. The Firm also failed timely to disclose that it had been named a respondent in an administrative disciplinary proceeding initiated by the Texas State Board of Public Accountancy ("Texas Board") in October 2011, or that the proceeding had been concluded on January 19, 2012. Madsen was aware of each of these reportable events at the times they occurred. However, the Firm did not file a Form 3

³⁷ PCAOB Rule 2203, *Special Reports*.

³⁸ Andersen was a defendant in *SEC v. Exotics.com, Inc.*, Civ. Act. No. 2:05-cv-00531-PMP-GWF (D. Nev. filed Apr. 25, 2005).

³⁹ L. Rex Andersen, CPA, Permanently Enjoined For Role in Penny Stock and Accounting Fraud, SEC Litigation Rel. No. 21519 (May 6, 2010).

⁴⁰ *L. Rex Andersen, CPA*, Exchange Act Rel. No. 62262 (Order Instituting Proceedings and Imposing Temporary Suspension, June 10, 2010).

⁴¹ See PCAOB Form 3 (Special Report), at Item 2.8 (requires disclosure of certain legal proceedings involving a partner, shareholder, principal, owner or audit manager of a firm); Item 2.10 (requires disclosure that certain legal proceedings involving a partner, shareholder, principal, owner or audit manager of a firm have concluded).

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reporting the events relating to the Texas Board's proceeding until June 26, 2012, more than thirty days after the events' occurrences.⁴²

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 Respondents' Offers. Accordingly, it is hereby ORDERED that:

- A. Pursuant to Section 105(c)(4)(E) of the Act and PCAOB Rule 5300(a)(5), Madsen & Associates CPAs, Inc. and Ted A. Madsen, CPA are hereby censured;
- B. Pursuant to Section 105(c)(4)(B) of the Act and PCAOB Rule 5300(a)(2), Ted A. Madsen, CPA is barred from being an associated person of a registered public accounting firm, as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(i);⁴³
- C. After two (2) years from the date of this Order, Ted A. Madsen, CPA may file a petition, pursuant to PCAOB Rule 5302(b), for Board consent to associate with a registered public accounting firm;
- D. Pursuant to Section 105(c)(4)(A) of the Act and PCAOB Rule 5300(a)(1), the registration of Madsen & Associates CPAs, Inc. is revoked; and

⁴² See *id.*, at Item 2.7 (requires disclosure of certain legal proceedings against a firm brought by a governmental entity or in an administrative or disciplinary proceeding other than a PCAOB disciplinary proceeding); Item 2.10 (requires disclosure that certain legal proceedings against a firm brought by a governmental entity or in an administrative or disciplinary proceeding other than a PCAOB disciplinary proceeding have concluded).

⁴³ As a consequence of the bar, the provisions of Section 105(c)(7)(B) of the Act will apply with respect to Madsen. Section 105(c)(7)(B) of the Act provides that "[i]t shall be unlawful for any person that is suspended or barred from being associated with a registered public accounting firm under this subsection willfully to become or remain associated with any issuer, broker, or dealer in an accountancy or a financial management capacity, and for any issuer, broker, or dealer that knew, or in the exercise of reasonable care should have known, of such suspension or bar, to permit such an association, without the consent of the Board or the Commission."

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- E. After two (2) years from the date of this Order, Madsen & Associates CPAs, Inc. may reapply for registration by filing an application pursuant to PCAOB Rule 2101.

ISSUED BY THE BOARD.

/s/ Phoebe W. Brown

Phoebe W. Brown
Secretary

January 15, 2015