
ORDER INSTITUTING DISCIPLINARY
PROCEEDINGS, MAKING FINDINGS,
AND IMPOSING SANCTIONS

In the Matter of Walker & Armstrong LLP,

Respondent.

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) PCAOB Release No. 105-2015-020

) July 9, 2015
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By this Order, the Public Company Accounting Oversight Board ("Board" or "PCAOB") is (1) censuring the registered public accounting firm Walker & Armstrong LLP ("Walker & Armstrong," "Firm," or "Respondent"); (2) imposing upon the Firm a civil money penalty in the amount of \$7,500; and (3) in the event the Board grants any future registration application by the Firm,¹ requiring the Firm to undertake certain remedial measures directed toward satisfying independence criteria applicable to audits of brokers and dealers. The Board is imposing these sanctions on the basis of its findings that the Firm violated a rule of the Securities and Exchange Commission ("Commission") in connection with two audits of a broker-dealer client as a result of preparing financial statements that the broker-dealer filed with the Commission and thus impairing the Firm's independence.

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 ("Act"), and PCAOB Rule 5200(a)(1) against Respondent.

II.

In anticipation of the institution of these proceedings and pursuant to PCAOB Rule 5205, Respondent submitted an Offer of Settlement ("Offer") that the Board has

¹ The Firm has filed a Form 1-WD seeking leave to withdraw from registration with the Board, which the Board has determined to grant as of the date of this Order.



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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 Respondent and the subject matter of these proceedings, which is admitted, Respondent consents to the entry of this Order Instituting Disciplinary Proceedings, Making Findings, and Imposing Sanctions ("Order") as set forth below.²

III.

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

A. Respondent

1. Walker & Armstrong is a registered public accounting firm with offices in Phoenix, Tucson, and Carefree, Arizona. At all relevant times, the Firm was licensed by the Arizona State Board of Accountancy (registration no. 375). The Firm, formed in 1971, is registered with the Board pursuant to Section 102 of the Act and Board rules.

B. Summary

2. Walker & Armstrong prepared the financial statements for a broker-dealer audit client ("Broker-Dealer") for the years ended December 31, 2012 and December 31, 2013. As a result, the Firm was not independent of the Broker-Dealer under auditor independence criteria established by the Commission and made applicable by Exchange Act Rule 17a-5(f)(3) to audits of brokers and dealers.³ The Firm nevertheless audited both sets of financial statements and issued audit reports that the Broker-Dealer

² The findings herein are made pursuant to Respondent's Offer and are not binding on any other person or entity in this or any other proceeding.

³ Exchange Act Rule 17a-5, referenced throughout this Order as "Rule 17a-5," is found at 17 C.F.R. § 240.17a-5. The rule provisions set out herein are those in effect during, and applicable to, the relevant conduct. On July 30, 2013, the Commission adopted certain amendments to Rule 17a-5. See Broker-Dealer Reports, SEC Exchange Act Release No. 34-70073 (July 30, 2013), 78 Fed. Reg. 51910 (Aug. 21, 2013). Among other things, the amendments to Rule 17a-5 require that audits of brokers and dealers be performed in accordance with PCAOB standards, effective for audits of fiscal years ending on or after June 1, 2014. In addition, Rule 17a-5 provides that the auditor must be independent in accordance with Rule 2-01 of Commission Regulation S-X. At the time of the relevant conduct, that requirement was set out in Rule 17a-5(f)(3). It is now set out in Rule 17a-5(f)(1).

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included with the financial statements it filed with the Commission. In each of the audit reports, the Firm represented that the audit had been performed in accordance with Generally Accepted Auditing Standards ("GAAS"). Because GAAS requires independence, however, each of those representations violated Rule 17a-5(i), which required the audit report to state whether the audit was made in accordance with GAAS.

C. Respondent Violated a Commission Rule

3. Rule 17a-5(d)(1) requires, among other things, that "[e]very broker or dealer registered pursuant to section 15 of the [Securities Exchange] Act [of 1934] shall file annually, on a calendar or fiscal year basis, a report which shall be audited by an independent public accountant." Rule 17a-5(d)(2) states that "[t]he annual audited report" filed by a registered broker or dealer, among other things, "shall contain a Statement of Financial Condition . . . , a Statement of Income, a Statement of Cash Flows, a Statement of Changes in Stockholders' or Partners' or Sole Proprietor's Equity, and [a] Statement of Changes in Liabilities Subordinated to Claims of General Creditors."

4. Rule 17a-5(e)(1)(i) states: "An audit shall be conducted by a public accountant who shall be in fact independent as defined in paragraph (f)(3) of this section herein, and he shall give an opinion covering the statements filed pursuant to paragraph (d)" Rule 17a-5(f)(3) states: "An accountant shall be independent in accordance with the provisions of § 210.2-01(b) and (c) of this chapter."

5. Rule 17a-5(g) requires that "[t]he audit shall be made in accordance with generally accepted auditing standards." Rule 17a-5(i) requires that "[t]he accountant's report shall . . . [s]tate whether the audit was made in accordance with generally accepted auditing standards."

6. GAAS requires auditors to maintain strict independence from their audit clients.⁴ "[I]f an auditor's report states that its audit was in accordance with GAAS when the auditor was not independent, then it has violated Rule 17a-5(i)."⁵

⁴ AU-C Section 200.15-.16, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*. References herein to GAAS are to the versions of the auditing standards that were applicable to audits of brokers and dealers at the time of the audit at issue here.

⁵ *Rosenberg Rich Baker Berman & Company*, Exchange Act Release No. 69765, 2013 WL 2898032, at *4 (June 14, 2013).



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7. Pursuant to Rule 17a-5(f)(3), certain of the Commission's auditor independence criteria described in Rules 2-01(b) and (c) of Regulation S-X⁶ apply to audits of brokers and dealers.⁷ The applicable provisions include Rule 2-01(c)(4), which states in part:

An accountant is not independent if, at any point during the audit and professional engagement period, the accountant provides the following non-audit services to an audit client:

(i) *Bookkeeping or other services related to the accounting records or financial statements of the audit client.* Any service, unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements, including:

...

(B) Preparing the audit client's financial statements that are filed with the Commission or that form the basis of financial statements filed with the Commission

8. The Firm served as the auditor of the Broker-Dealer's December 31, 2012 financial statements, as well as its December 31, 2013 financial statements. At all relevant times, the Broker-Dealer was a "broker" and "dealer," as defined in Section 110 of the Act and PCAOB Rules 1001(b)(iii) and 1001(d)(iii), and was not an "issuer," as defined in Section 2(a)(7) of the Act and PCAOB Rule 1001(i)(iii).

9. In February 2013, the Broker-Dealer filed with the Commission a Form X-17A-5 Part III for the year ended December 31, 2012. Included in that filing was an audit report signed by the Firm dated February 25, 2013. That report stated, among other

⁶ 17 C.F.R. Part 210.

⁷ Not all independence criteria described in Rule 2-01(c) apply to audits of brokers and dealers. As the Commission has explained, those audits "are not subject to the partner rotation requirements or the compensation requirements of the Commission's independence rules [Rules 2-01(c)(6) and (c)(8)] because the statute mandating those requirements is limited to issuers," and they "are not subject to the audit committee pre-approval requirements or the cooling-off period requirements for employment [Rules 2-01(c)(7) and (c)(2)(iii)(B)] because those requirements only reference issuers." See Exchange Act Release No. 34-70073 at II.E.



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things, that the Firm audited the Broker-Dealer's financial statements "in accordance with auditing standards generally accepted in the United States of America."

10. Firm staff completed an "Engagement Acceptance and Continuance Form" in connection with the audit of the Broker-Dealer's December 31, 2012 financial statements ("2012 Audit"). That form included a pre-printed item reading, "What services does the financial institution desire from our firm?" Firm staff added a checkmark under "No" alongside the pre-printed sub-item reading, "Preparation of financial statements," as well as a note that the Broker-Dealer "determines groupings and note disclosure language with recommendations by [Walker & Armstrong]."

11. Firm staff also completed a work paper titled "Understanding the Entity and Identifying Risks," which contained a pre-printed item calling for an identification of "significant accounting policies," specialized or new "accounting standards," and "any other issues related to the application of GAAP." In response to that item, Firm staff added a note reading, in part: "SEC independence rules, PCAOB audit standards (possible in the near future)" (emphasis added).

12. Firm staff obtained from the Broker-Dealer in January and February 2013 various documents including a trial balance, a balance sheet as of December 31, 2012, and an income statement for the year ended December 31, 2012. The documents obtained from the Broker-Dealer also included four Forms X-17A-5 Part IIA—one for each of the four quarters of 2012—that Firm staff understood had been filed by the Broker-Dealer with the Financial Industry Regulatory Authority ("FINRA"), that bore the headers "FOCUS Report (Financial and Operational Combined Uniform Single Report)," and that contained quarterly financial statements ("Quarterly FOCUS Reports"). Firm staff also obtained from the Broker-Dealer in connection with each Quarterly FOCUS Report a set of documents containing related information for that quarter—specifically, a trial balance, a sales report, and a financial statement document consisting of a "Balance Sheet," a "Statement of Operations," and a "Calculation of Net Capital."

13. On February 5, 2013, Firm staff emailed the Broker-Dealer proposed groupings of asset, liability, income, and expense items under captions and into line items for inclusion in the financial statements to be filed with the Commission. Firm staff noted in the email that the attached groupings matched those used in connection with the previous year's financial statements filed by the Broker-Dealer with the Commission. By February 15, 2013, Broker-Dealer management had communicated approval of those groupings to Firm staff.

14. Firm staff used the above documents obtained from and groupings approved by the Broker-Dealer to prepare the Statement of Financial Condition as of



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December 31, 2012, as well as the Statement of Income for the year ended December 31, 2012, filed by the Broker-Dealer with the Commission in February 2013.

15. In preparing the groupings approved by the Broker-Dealer, and thereafter the Statement of Financial Condition and Statement of Income filed by the Broker-Dealer with the Commission, Firm staff aggregated line items, deleted captions and line items, and changed line item descriptions as compared to corresponding information in the documents obtained from the Broker-Dealer.

16. Firm staff also prepared the Statement of Changes in Partners' Capital and Statement of Cash Flows for the year ended December 31, 2012, which were filed by the Broker-Dealer with the Commission in February 2013.

17. Firm staff provided the Broker-Dealer with a set of draft financial statements on February 22, 2013 for management approval.

18. Following the 2012 Audit, Board inspection staff conducted a review of certain aspects of the 2012 Audit. On January 21, 2014, the Firm received a comment form issued by Board inspection staff in connection with that review. The comment form set out the staff's finding that the Firm had failed to maintain auditor independence under Rule 2-01(c)(4)(i) of Regulation S-X because it had prepared financial statements of the Broker-Dealer. Firm staff discussed the comment form and the finding therein with Broker-Dealer management personnel.

19. In February 2014, the Broker-Dealer filed with the Commission a Form X-17A-5 Part III for the year ended December 31, 2013. Included in that filing was an audit report signed by the Firm dated February 26, 2014. That report stated, among other things, that the Firm audited the Broker-Dealer's financial statements "in accordance with auditing standards generally accepted in the United States of America."

20. Firm staff completed an "Engagement Acceptance and Continuance Form" in connection with the audit of the Broker-Dealer's December 31, 2013 financial statements ("2013 Audit"). Like the form completed in connection with the previous year's audit, this form included a pre-printed item reading, "What services does the financial institution desire from our firm?," as well as a checkmark added by Firm staff under "No" alongside the pre-printed sub-item reading, "Preparation of financial statements." Firm staff also added a note reading, "[Broker-Dealer] prepares."

21. Firm staff also completed a work paper titled "Understanding the Entity and Identifying Risks." Like the form completed in connection with the 2012 Audit, this form contained a pre-printed item calling for an identification of "significant accounting policies," specialized or new "accounting standards," and "any other issues related to



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the application of GAAP." Firm staff added the same note in response to that item as had been added to the previous year's form: "SEC independence rules, PCAOB audit standards (possible in the near future)" (emphasis added).

22. In January and February 2014, Firm staff obtained from the Broker-Dealer in connection with the 2013 Audit substantially the same types of documents obtained the previous year in connection with the 2012 Audit.

23. In addition, on February 6, 2014, Firm staff obtained from the Broker-Dealer a draft set of December 31, 2013 financial statements, including Statements of Financial Condition, Income, Changes in Partners' Capital, and Cash Flows, as well as a draft set of notes to those financial statements, for filing with the Commission. Firm staff thereafter identified certain aspects of the financial statements including notes that, in their view, should be revised. Firm staff discussed and obtained approval for those proposed revisions during a meeting on February 24, 2014 with the Broker-Dealer's chief financial officer; made those revisions in the electronic copy of the draft financial statements that the Firm had received; provided the Broker-Dealer with a copy of that revised set on February 26, 2014 for management approval; and generated from that Firm-revised set the final version of the financial statements including notes, which were later filed by the Broker-Dealer with the Commission.

24. The revisions made by Firm staff to the financial statements and notes drafted by and obtained from the Broker-Dealer included changes to 15 of 31 line item amounts in the Statement of Financial Condition and Statement of Income; nine of 24 line item descriptions and 16 of 24 line item amounts in the Statement of Cash Flows; and 13 of 43 paragraphs in the notes to the financial statements (including, for example, the deletion of one paragraph altogether, the addition of a tabular presentation, and the disaggregation on a year-by-year basis of information concerning the timing of certain future payments due from the Broker-Dealer).

25. Firm staff also asked Broker-Dealer management personnel to make the same revisions to the Broker-Dealer's own electronic copy of the draft financial statements, and then to email to the Firm a copy of that client-revised set for the Firm's records. Broker-Dealer management personnel did so.

26. Firm staff prepared the Broker-Dealer's December 31, 2013 financial statements, including notes, notwithstanding the fact that Firm staff took different steps to do so than it had in the previous year and believed that those steps would not impair the Firm's independence.

27. As a result of the Firm's conduct—both in preparing the December 31, 2012 financial statements before being notified by Board inspection staff that such

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preparation impaired its independence, and in preparing the December 31, 2013 financial statements after that notification—the Firm was not independent of the Broker-Dealer under the independence criteria established by the Commission in Rule 2-01(c)(4) of Regulation S-X, which Rule 17a-5 made applicable to the audits of the Broker-Dealer's financial statements. As the Commission explained in adopting Rule 2-01(c)(4), providing such services for an audit client "impairs the auditor's independence because the auditor will be placed in the position of auditing the firm's work when auditing the client's financial statements. . . . In addition, keeping the books is a management function, the performance of which leads to an inappropriate mutuality of interests between the auditor and the audit client."⁸

28. The Firm violated Rule 17a-5(i) by representing in its audit reports that it had performed the audits of the Broker-Dealer's December 31, 2012 financial statements and December 31, 2013 financial statements in accordance with GAAS when in fact, because of the independence impairments described above, the audits had not been performed in accordance with GAAS. Those violations constituted violations of the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto.

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:

- A. Pursuant to Section 105(c)(4)(E) of the Act and PCAOB Rule 5300(a)(5), the Firm is censured.
- 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 \$7,500 is imposed upon the Firm. 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. The Firm shall pay this civil money penalty within ten (10) days of the issuance of this Order by (1) wire transfer pursuant to instructions

⁸ *Revision of the Commission's Auditor Independence Requirements*, Exchange Act Release No. 43602 (November 21, 2000) at IV.D.4.b(i).

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provided 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 Firm 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.

C. Pursuant to Section 105(c)(4)(G) of the Act and PCAOB Rule 5300(a)(9), the Firm is required, should the Board grant any future application of the Firm for registration:

1. within ninety (90) days from the date the Board grants any future application of the Firm for registration ("Future Registration Date"), to establish policies and procedures, or revise and/or supplement existing policies and procedures, for the purpose of providing the Firm with reasonable assurance of compliance with applicable independence requirements, including those requirements of Rule 2-01 of Regulation S-X applicable to an SEC Registered Broker-Dealer Engagement (defined to mean an engagement to provide a report—whether an audit report, an examination report, or a review report—required under paragraph (d)(1)(i)(C) of Rule 17a-5, as amended);

2. within ninety (90) days from the Future Registration Date, to establish a policy of ensuring training, whether internal or external, on an annual or more frequent regular basis, concerning applicable independence requirements, including those requirements of Rule 2-01 of Regulation S-X applicable to an SEC Registered Broker-Dealer Engagement, of any Firm audit personnel who participate in any way in the planning or performing of any SEC Registered Broker-Dealer Engagement;

3. within ninety (90) days from the Future Registration Date and before the Firm's commencement of any SEC Registered Broker-Dealer Engagement, to ensure training pursuant to the policy described in paragraph C(2) above on at least one occasion;

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4. to provide a copy of this Order—

a. within (30) days from the Future Registration Date, to all audit personnel employed by, or associated with (as defined in PCAOB Rule 1001(p)(i)), the Firm as of the Future Registration Date,

b. within (30) days from the Future Registration Date, to any client of the Firm as of the Future Registration Date for which the Firm has performed or has been engaged to perform an SEC Registered Broker-Dealer Engagement,

c. before the commencement of any SEC Registered Broker-Dealer Engagement, to any future client for which the Firm is engaged within three (3) years of the date of this Order to perform such an engagement; and

5. to certify in writing to the Director of the Division of Enforcement and Investigations, Public Company Accounting Oversight Board, 1666 K Street, N.W., Washington D.C. 20006, the Firm's compliance with paragraphs C(1) through C(4)(b) above. The certification shall identify the undertakings, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Firm shall submit such certification within one hundred twenty (120) days from the Future Registration Date. The Firm shall also submit such additional evidence of and information concerning compliance as the staff of the Division of Enforcement and Investigations may reasonably request.

ISSUED BY THE BOARD.

/s/ Phoebe W. Brown

Phoebe W. Brown
Secretary

July 9, 2015