

Report on
2016 Inspection of PricewaterhouseCoopers LLP
(Headquartered in New York, NY)

Issued by the
Public Company Accounting Oversight Board

December 19, 2017

THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT

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SECTIONS 104(g)(2) AND 105(b)(5)(A)
OF THE SARBANES-OXLEY ACT OF 2002**



2016 INSPECTION OF PRICEWATERHOUSECOOPERS LLP

Preface

In 2016, the Public Company Accounting Oversight Board ("PCAOB" or "the Board") conducted an inspection of the registered public accounting firm PricewaterhouseCoopers LLP ("the Firm") pursuant to the Sarbanes-Oxley Act of 2002 ("the Act").

Inspections are designed and performed to provide a basis for assessing the degree of compliance by a firm with applicable requirements related to auditing issuers. For a description of the procedures the Board's inspectors may perform to fulfill this responsibility, see Part I.D of this report (which also contains additional information concerning PCAOB inspections generally). The inspection included reviews of portions of selected issuer audits. These reviews were intended to identify whether deficiencies existed in the reviewed work, and whether such deficiencies indicated defects or potential defects in the Firm's system of quality control over audits. In addition, the inspection included a review of policies and procedures related to certain quality control processes of the Firm that could be expected to affect audit quality.

The Board is issuing this report in accordance with the requirements of the Act. The Board is releasing to the public Part I of the report, portions of Appendix B, and Appendix C. Appendix B consists of the Firm's comments, if any, on a draft of the report. If the nonpublic portions of the report discuss criticisms of or potential defects in the Firm's system of quality control, those discussions also could eventually be made public, but only to the extent the Firm fails to address the criticisms to the Board's satisfaction within 12 months of the issuance of the report. Appendix C presents the text of the paragraphs of the auditing standards that are referenced in Part I.A in relation to the description of auditing deficiencies there.

Note on this report's citations to auditing standards: On March 31, 2015, the PCAOB adopted a reorganization of 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). The reorganization became effective as of December 31, 2016. Citations in this report reference the reorganized PCAOB auditing standards.

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EXECUTIVE SUMMARY

This summary sets out certain key information from the 2016 inspection of PricewaterhouseCoopers LLP ("the Firm"). The inspection procedures included reviews of portions of 53 issuer audits performed by the Firm and a review of the Firm's audit work on three other issuer audit engagements in which the Firm played a role but was not the principal auditor. Forty-nine of the 56 engagements were integrated audits of both internal control and the financial statements. Part I.C of this report provides certain demographic information about the audits inspected and Part I.D describes the general procedures applied in the PCAOB's 2016 inspections of annually inspected registered firms.

The inspection team identified matters that it considered to be deficiencies in the performance of the work it reviewed. In 11 audits, certain of the deficiencies identified were of such significance that it appeared to the inspection team that the Firm, at the time it issued its audit report, had not obtained sufficient appropriate audit evidence to support its opinion that the financial statements were presented fairly, in all material respects, in conformity with the applicable financial reporting framework and/or its opinion about whether the issuer had maintained, in all material respects, effective internal control over financial reporting ("ICFR"). These deficiencies are described in Part I.A of the report.

Effects of Audit Deficiencies on Audit Opinions

Of the 11 issuer audits that appear in Part I.A, deficiencies in nine audits relate to testing controls for purposes of the ICFR opinion, and deficiencies in ten audits relate to the substantive testing performed for purposes of the opinion on the financial statements, as noted in the table below.

	Number of Audits
Audits for which deficiencies included in Part I.A related to both the financial statement audit and the ICFR audit	<u>8 Audits</u> : Issuers A, B, C, E, F, G, J, and K
Audits for which deficiencies included in Part I.A related to the ICFR audit only	<u>1 Audit</u> : Issuer H

	Number of Audits
Audits for which deficiencies included in Part I.A related to the financial statement audit only	<u>2 Audits</u> : Issuers D and I
Total	11

Most Frequently Identified Audit Deficiencies

The following table lists, in summary form, the types of deficiencies that are included most frequently in Part I.A of this report. A general description of each type is provided in the table; the description of each deficiency in Part I.A contains more specific information about the individual deficiency. The table includes only the three most frequently identified deficiencies that are in Part I.A of this report and is not a summary of all deficiencies in Part I.A.

Issue	Part I.A Audits
Failure to sufficiently test the design and/or operating effectiveness of controls that the Firm selected for testing	<u>7 Audits</u> : Issuers A, B, C, E, F, H, and J
Failure to sufficiently evaluate significant assumptions that the issuer used in developing an estimate	<u>7 Audits</u> : Issuers A, B, C, E, F, I, and K
Failure to perform sufficient testing related to an account or significant portion of an account or to address an identified risk	<u>5 Audits</u> : Issuers B, D, F, G, and J

Areas in which Audit Deficiencies Were Most Frequently Identified

The following table lists, in summary form, the financial statement accounts or auditing areas in which the deficiencies that are included in Part I.A of this report most frequently occurred. The table includes only the three most frequently identified areas that are in Part I.A of this report and is not a summary of all deficiencies in Part I.A.

Area	Part I.A Audits
Revenue, including accounts receivable, deferred revenue, and allowances	<u>6 Audits</u> : Issuers A, B, D, F, G, and H
Inventory and Related Reserves	<u>3 Audits</u> : Issuers B, D, and J

Area	Part I.A Audits
Fixed Assets	<u>3 Audits:</u> Issuers C, E, and F

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's staff ("the inspection team") conducted primary procedures¹ for the inspection from November 2015 to March 2017. The inspection team performed field work at the Firm's National Office and at 29 of its approximately 65 U.S. practice offices.

A. Review of Audit Engagements

The inspection procedures included reviews of portions of 53 issuer audits performed by the Firm and a review of the Firm's audit work on three other issuer audit engagements in which the Firm played a role but was not the principal auditor. The inspection team identified matters that it considered to be deficiencies in the performance of the work it reviewed. One of the deficiencies relates to auditing an aspect of an issuer's financial statements that the issuer restated after the primary inspection procedures.² In two of the audits described below, after the primary inspection procedures, the Firm revised its opinion on the effectiveness of the issuer's internal control over financial reporting to express an adverse opinion.

The descriptions of the deficiencies in Part I.A of this report include, at the end of the description of each deficiency, references to specific paragraphs of the auditing standards that relate to those deficiencies. The text of those paragraphs is set forth in

¹ For this purpose, the time span for "primary procedures" includes field work, other review of audit work papers, and the evaluation of the Firm's quality control policies and procedures through review of documentation and interviews of Firm personnel. The time span does not include (1) inspection planning, which may commence months before the primary procedures, and (2) inspection follow-up procedures, wrap-up, analysis of results, and the preparation of the inspection report, which generally extend beyond the primary procedures.

² The 2016 inspection did not include review of any additional audit work related to the restatement.

Appendix C to this report. The references in this sub-Part include only standards that primarily relate to the deficiencies; they do not present a comprehensive list of every auditing standard that applies to the deficiencies. Further, certain broadly applicable aspects of the auditing standards that may be relevant to a deficiency, such as provisions requiring due professional care, including the exercise of professional skepticism; the accumulation of sufficient appropriate audit evidence; and the performance of procedures that address risks, are not included in the references to the auditing standards in this sub-Part, unless the lack of compliance with these standards is the primary reason for the deficiency. These broadly applicable provisions are described in Part I.B of this report.

Certain of the deficiencies identified were of such significance that it appeared to the inspection team that the Firm, at the time it issued its audit report, had not obtained sufficient appropriate audit evidence to support its opinion that the financial statements were presented fairly, in all material respects, in conformity with the applicable financial reporting framework and/or its opinion about whether the issuer had maintained, in all material respects, effective ICFR. In other words, in these audits, the auditor issued an opinion without satisfying its fundamental obligation to obtain reasonable assurance about whether the financial statements were free of material misstatement and/or the issuer maintained effective ICFR.

The fact that one or more deficiencies in an audit reach this level of significance does not necessarily indicate that the financial statements are misstated or that there are undisclosed material weaknesses in ICFR. It is often not possible for the inspection team, based only on the information available from the auditor, to reach a conclusion on those points.

Whether or not associated with a disclosed financial reporting misstatement, an auditor's failure to obtain the reasonable assurance that the auditor is required to obtain is a serious matter. It is a failure to accomplish the essential purpose of the audit, and it means that, based on the audit work performed, the audit opinion should not have been issued.³

³ Inclusion in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the firm's attention. Depending upon the circumstances, compliance with PCAOB 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

The audit deficiencies that reached this level of significance are described in Parts I.A.1 through I.A.11, below.

Audit Deficiencies

A.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 on the effectiveness of ICFR –

- To determine the fair value of certain significant acquired intangible assets, the issuer prepared cash-flow forecasts for each of the acquired company's product categories and then allocated the forecasted cash flows among these intangible assets based on the expected lifecycles of the products ("cash-flow allocations"). The Firm's procedures related to the valuation of these assets were insufficient in the following respects –
 - The Firm selected for testing a control that included a review of significant assumptions underlying the cash-flow forecasts and the cash-flow allocations. The Firm failed to sufficiently test this control, as follows –
 - The Firm's procedures related to the aspect of the control that consisted of the control owner's review of the forecasted selling, general, and administrative ("SG&A") expenses were insufficient. Specifically –

prevent reliance on its previously expressed audit opinions. The Board expects that firms will comply with these standards, and an inspection may include a review of the adequacy of a firm's compliance with these requirements, either with respect to previously identified deficiencies or deficiencies identified during that inspection. 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.

- The Firm failed to evaluate whether the control operated at an appropriate level of precision since the control owner reviewed the forecasted amounts at an operating level, which was higher than the product-category level. (AS 2201.42 and .44)
- The control owner's review included comparing the forecasted amounts to the acquired company's historical SG&A expenses after taking into account anticipated changes in the business. The Firm's procedures to test this aspect of the control were limited to (1) reading a memorandum that the issuer prepared prior to the acquisition that focused only on sales and cost of sales and (2) inquiring of management. (AS 2201.42 and .44)
- The Firm's procedures to test the control owner's review of the reasonableness of the cash-flow allocations were limited to inquiry and attendance at a meeting that included a discussion of the lifecycles of existing products and the timing of new product releases. The Firm failed to ascertain and evaluate the specific procedures that the control owner performed in assessing the reasonableness of the specific percentages that the issuer used to allocate revenue projections over the expected product lifecycles. (AS 2201.42 and .44)
- The Firm failed to perform sufficient substantive procedures to test the valuation of the acquired intangible assets. Specifically –
 - The Firm's procedures to evaluate the reasonableness of the forecasted SG&A expenses consisted of comparing the forecasted SG&A expenses as a percentage of forecasted revenue in the first three years of the forecast to (1) the acquired company's actual percentage for the prior year and (2) market participant averages. The SG&A percentages for the first three years of the forecast were significantly lower

than both the prior-year percentage and the market participant averages, but the Firm's procedures to address the differences were limited to inquiring of management regarding anticipated changes in the business and noting that the anticipated changes were consistent with other transactions in the same industry. The Firm's procedures to evaluate the reasonableness of the forecasted SG&A expenses for any of the periods beyond the first three years were limited to inquiry. (AS 2502.26, .28, .31, and .36)

- The Firm's procedures to test the cash-flow allocations were limited to inquiring of management and understanding the historical duration of product lifecycles. The Firm failed to evaluate the reasonableness of the specific percentages that the issuer used to allocate revenue projections over the expected product lifecycles. (AS 2502.26, .28, .31, and .36)
- To determine whether the prices were fixed and determinable for certain product groups, the issuer used a complex model to estimate prices that included assumptions about possible future returns and concessions. The Firm identified that the issuer had made significant changes to the model in the current year and that revenue for a significant number of additional product groups were now accounted for based upon this model. The issuer performed an analysis to evaluate whether the estimated prices for these product groups were comparable to the actual prices that the issuer realized and, therefore, to support that product groups accounted for using this model could continue using this model. The Firm's procedures related to this revenue were insufficient in the following respects –
 - The Firm failed to perform sufficient procedures to address the risks of material misstatement related to recognizing revenue using this model. Specifically, the Firm failed to identify and test any controls that addressed, and failed to perform any substantive procedures to address, (1) which products were assigned to each product group and, therefore, which products should be accounted for using this model and (2) the accuracy of coding products to the correct groups. (AS 2201.39; AS 2501.11)

- The Firm selected for testing a control over the analysis, but failed to sufficiently test this control, as its procedures were limited to (1) obtaining the analysis and noting that all product groups for which revenue was recognized using the model were included in the analysis and that the aggregate differences between the estimated price and actual sales price for each product group were immaterial and (2) testing the mathematical accuracy of the analysis. The Firm failed to test the aspects of the control related to (1) the control owner's review of the accuracy and completeness of the reports used in the analysis and (2) the control owner's evaluation of the qualitative factors that could affect the issuer's ability to reasonably determine the estimated price. (AS 2201.42 and .44)
- The Firm failed to perform any substantive procedures to evaluate the reasonableness of the qualitative factors used in the analysis. (AS 2501.11)

A.2 Issuer B

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 on the effectiveness of ICFR –

- The Firm's procedures related to the valuation of goodwill for one of the issuer's reporting units were insufficient. Specifically –
 - The Firm failed to perform sufficient substantive procedures to evaluate the reasonableness of the forecast that the issuer used in the goodwill impairment analysis, as it failed to sufficiently evaluate information that it obtained that appeared to be inconsistent with the forecast, as described below.
 - The Firm compared the forecasted revenue growth rates to the issuer's three-year historical growth rate, noting significant differences. The Firm's procedures to evaluate these differences were insufficient, as they were limited to inquiring of management and obtaining a signed purchase

commitment for a contract that had been deferred indefinitely. (AS 2502.26, .28, .31, and .36; AS 2810.03)

- The Firm compared the issuer's fourth-quarter forecast to the actual results for that quarter, and it identified significant differences. The Firm inquired as to the reasons for the differences, but failed to evaluate the implications of the differences. (AS 2502.26, .28, .31, and .36; AS 2810.03)
- The issuer included revenue from anticipated large international contracts in its forecast. In evaluating the reasonableness of the revenue forecast, the Firm failed to consider that (1) the issuer had disclosed delays and uncertainties related to international contracts and (2) historically, the issuer had obtained only a small number of contracts of comparable size to the anticipated international contracts, and all of those were with domestic customers. (AS 2502.26, .28, and .36; AS 2810.03)
- The Firm failed to evaluate the significant difference between the issuer's implied earnings multiple based on management's forecasts and the average earnings multiples of comparable companies that the Firm had obtained. (AS 2502.26, .28, .31, and .36; AS 2810.03)
- The Firm selected for testing a control that consisted of the preparation and review of goodwill impairment tests. The objectives of this control included assessing the reasonableness of the underlying revenue forecast and determining whether the revenue forecast was consistent with recent trends and expected changes. The Firm failed to sufficiently test these aspects of the control, as the Firm did not evaluate whether, or how, the control owners, when preparing and reviewing the revenue forecast, considered the potentially inconsistent information that is described above. (AS 2201.44)

- The issuer used historical and projected usage reports to identify slow-moving and obsolete inventory, and it evaluated this inventory to determine whether an allowance was required. The Firm's procedures related to the allowance were insufficient. Specifically –
 - The Firm selected for testing one control over the allowance for obsolete inventory that consisted of management's quarterly evaluation of the allowance calculation. The Firm, however, failed to identify and test any controls over the accuracy and completeness of the underlying historical and projected usage reports. (AS 2201.39)
 - For one of the issuer's divisions, the Firm's substantive testing of the allowance for obsolete inventory consisted of (1) inquiring of management and (2) comparing the three-year average obsolete inventory expense to the current year-end allowance balance and discussing any significant differences with management. The Firm, however, failed to obtain evidence that the historical average expense could reasonably be expected to be predictive of the issuer's allowance at the year end. (AS 2501.12)
- For two divisions, the issuer used cycle counts to determine the quantities of its inventory. The Firm's procedures to test the existence of, and the controls over the existence of, raw materials inventory for these divisions were insufficient in the following respects –
 - The Firm failed to perform any procedures to test the accuracy and completeness of the cycle-count accuracy reports, which the issuer used to assess the reliability of the cycle-count process. (AS 2201.39; AS 2510.11)
 - The Firm's procedures to test the frequency of the counts in the cycle-count program were limited to selecting items at the locations selected for testing and documenting either that the selected items were counted during one cycle count or that the items were included in the perpetual inventory listing. These procedures failed to address whether the selected items were counted as frequently

as required under the cycle-count program. (AS 2201.44; AS 2510.11)

- The Firm failed to perform sufficient procedures related to the valuation of accounts receivable. The Firm selected for testing a control over the allowance for doubtful accounts that consisted of a review of the allowance. The Firm, however, failed to identify and test any controls over the accuracy and completeness of the accounts receivable aging report that was used in the operation of this control. In addition, the issuer used this report in determining the allowance, but the Firm failed to test the accuracy and completeness of the report. (AS 2201.39; AS 2501.11)

A.3 Issuer C

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

- The Firm failed to perform sufficient procedures related to the evaluation of oil and gas properties for possible impairment. Specifically –
 - The Firm selected for testing five controls to address risks related to assumptions underlying the forecasted cash flows that the issuer used in its evaluation. The important underlying assumptions included the future production, forecasted expense, and future development cost ("FDC") assumptions. The five controls consisted of (1) a review of the quarterly earnings, including a comparison of the issuer's current-quarter earnings to prior-quarter earnings, by segment; (2) an automated process to require approval for expenses, including development costs; (3) a procedure to determine the completeness of the FDCs that the issuer input into the system that it used to calculate the estimated cash flows; (4) the preparation and review of a quarterly reconciliation of changes in the issuer's oil and gas reserve volumes; and (5) an evaluation by an external specialist of the issuer's estimates of the reserves and net future revenue for all of the issuer's oil and gas properties. The Firm, however, failed to recognize that the controls it selected

for testing were not designed to address the reasonableness of the future production, forecasted expense, or FDC assumptions. (AS 2201.39)

- The issuer engaged an external specialist to evaluate the estimates of the reserves and net future revenue for all of the issuer's oil and gas properties. The Firm used the work of the specialist as evidence in performing its procedures. The Firm, however, failed to test the accuracy and completeness of the data that the issuer provided to the external specialist. (AS 1210.12)
- The Firm failed to sufficiently evaluate the reasonableness of the future production, forecasted expense, and FDC assumptions that the issuer used to determine the value of its oil and gas properties. The Firm's procedures to test these assumptions were limited to comparisons of the issuer's prior-year forecasts to the actual results. These procedures were insufficient, as the comparisons showed significant differences between the prior-year forecasts and actual results, but the Firm's procedures to evaluate the differences were limited to inquiry. (AS 2502.26, .28, and .36)
- The Firm's procedures to test controls over the valuation of derivative instruments were insufficient. The Firm selected for testing a control that consisted of a review of the calculation of the value of the derivative instruments, as well as the underlying inputs. The Firm's testing of this control was limited to inquiring of the preparer of the calculation, inspecting the documentation supporting the calculation, testing the mathematical accuracy of the calculation, comparing inputs to other documentation, and comparing the resulting valuation adjustment to journal entries. The Firm failed to ascertain and evaluate the nature of the activities that the control owner performed to review the calculation and underlying inputs, including the criteria that the control owner used to identify matters for follow up and whether any such matters were appropriately resolved. (AS 2201.42 and .44)

A.4. Issuer D

In this audit of a manufacturer of made-to-order equipment, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements –

- The issuer recognized the majority of its equipment revenue when the equipment was available for pickup or delivery ("completion date") and payment had been made. A significant portion of the equipment revenue was derived from bill-and-hold transactions whereby the issuer retained possession of the equipment after recognizing the associated revenue. Revenues from bill-and hold transactions in which the issuer had possession of the equipment at year end were multiple times the Firm's established materiality level. The Firm's tests of the majority of the issuer's equipment revenue were insufficient in the following respects –
 - The Firm identified fraud risks related to equipment revenue and, without any reliance on controls, performed certain substantive procedures intended specifically to address those risks. The Firm, however, designed most of those substantive procedures, including sampling procedures, to obtain only a low level of assurance, and the Firm in fact obtained only a low level of assurance from such procedures. (AS 2301.37 and .42)
 - To test revenue, the Firm selected for testing certain sales transactions that occurred throughout the year, including some bill-and-hold transactions, and it also performed cut-off testing for one significant category of revenue.
 - The Firm failed to sufficiently test the completion dates that it used in its cut-off and bill-and-hold testing, as its procedures were limited to obtaining the dates from the sales system, which the Firm did not test. (AS 1105.10)
 - The Firm identified a risk of misstatement related to the timing of revenue recorded in the 21-day periods before and after year end. The Firm's testing to address this identified

risk was insufficient, as it was limited to selections only from the last day of the year for only one customer. (AS 2301.08)

- In addition to the failure to test the completion dates described above, the Firm's testing of bill-and-hold transactions open at year end was insufficient in the following respects –
 - To test the occurrence of bill-and-hold transactions open at year end, the Firm performed a test of details by selecting a sample of equipment located in the issuer's storage facility. The Firm failed to perform any procedures to determine whether the equipment located in the issuer's storage facility represented all recorded bill-and-hold transactions open at the end of the year. (AS 2301.08)
 - The Firm failed to perform any procedures to test whether the issuer retained any performance obligations related to bill-and-hold transactions that were open as of year end. (AS 2301.08)
- The Firm tested the issuer's controls over the raw materials inventory cycle counts and planned for this testing to also provide substantive assurance. The Firm failed to perform sufficient procedures related to raw materials inventory. Specifically –
 - The Firm concluded that the issuer's cycle-count controls were ineffective during the first eight months of the year. The Firm determined that a portion of raw materials inventory was not counted in the four-month period between the remediation of the deficiencies in the issuer's cycle-count controls and the year end, which appeared to be in contravention of the issuer's policy that specified the frequency of the counts during the year. The Firm failed to evaluate the implications of this circumstance on the reliability of the cycle-count process. (AS 2301.32; AS 2510.11)
 - The Firm failed to test the configuration of the automated cycle-count program, or perform other procedures, to determine whether

all items were subject to counting in accordance with the issuer's cycle-count parameters. (AS 2301.19 and .21, AS 2510.11)

- The Firm performed attribute sampling to test the allowance for obsolete raw materials inventory for one significant location by making selections from the perpetual inventory listing and evaluating, based on production usage, whether each item selected was properly included in, or excluded from, the calculation of the inventory allowance. This procedure was insufficient in that the Firm's testing of each selected item was limited to inspecting the item's production usage as recorded in the issuer's inventory system, which the Firm did not test. (AS 1105.10)

A.5 Issuer E

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 ICFR, as it failed to perform sufficient procedures related to the valuation of certain equipment. Specifically –

- The Firm selected for testing a control that included reviews of an impairment analysis for equipment with indicators of potential impairment, including reviews of the estimated future cash flows associated with the equipment. The Firm failed to sufficiently test this aspect of the control, as it failed to evaluate the specific activities that the control owners performed to assess the reasonableness of the underlying assumptions regarding the frequency of customers' use of the equipment ("utilization") and the rate the issuer would charge for the use of the equipment ("pricing"), including the criteria that the control owners used to identify matters for follow up and whether those matters were appropriately resolved. (AS 2201.42 and .44)
- The Firm failed to sufficiently evaluate the reasonableness of significant assumptions underlying the estimated future cash flows that the issuer used to assess the possible impairment of substantially all of this equipment. Specifically –

- The Firm's procedures to evaluate the reasonableness of the utilization assumption consisted of (1) a comparison of the projected utilization to the issuer's historical utilization data (2) a comparison of the projected utilization to certain industry-wide expectations related to the demand for this type of equipment, and (3) inquiry of management regarding future expectations for its customer base. While the Firm noted that the issuer had experienced a significant change in its customer base during the time period covered by the historical data, and that the historical activity may not be indicative of future activity, it failed to perform additional procedures to test the projected utilization. In addition, the Firm failed to evaluate whether the issuer's utilization of its equipment correlated with the industry-wide data that it used for comparison. (AS 2501.11)
- The Firm's procedures to evaluate the reasonableness of the pricing assumptions beyond the second year in the forecast period consisted of a comparison of the projected pricing to the actual rates that the issuer charged its customers in a prior year. In evaluating the comparison, the Firm failed to take into account that the forecasts for prices of the products that the issuer's customers produced with the equipment after the second year in the forecast period were substantially below the level of the actual product prices during the prior year that was used for comparison. (AS 2501.11)
- The issuer identified certain equipment for which the carrying values exceeded the sum of the estimated future cash flows expected from the equipment; the issuer concluded, based on qualitative factors specific to each piece of equipment, that such equipment was not impaired. The Firm's procedures to evaluate each piece of this equipment were limited to a selection of the following: (1) reading the issuer's memorandum documenting its conclusion, (2) vouching the increase in net book value when the equipment was refurbished to support from the prior year during which it was refurbished, (3) reviewing the equipment's historical performance, (4) inquiring of management regarding its expectation of the equipment's future performance, and (5) inquiring of management

regarding the value of the components and parts of the equipment. The Firm failed to obtain sufficient evidence to evaluate the significant assumptions on which the issuer's conclusions were based. Specifically, the Firm failed to (1) evaluate the reasonableness of the expected increase in the remaining useful life of the equipment; (2) evaluate the reasonableness of the length of time that the issuer expected that contracts for the use of the equipment would be extended beyond their current end dates; and (3) test, beyond inquiry, the fair value of the components and parts of the equipment. (AS 2501.11)

A.6 Issuer F

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

- The Firm failed to perform sufficient procedures related to the evaluation of oil and gas properties for possible impairment. Specifically –
 - The Firm identified a likely source of potential misstatement related to the assumptions the issuer used in its evaluation of oil and gas properties. The Firm selected for testing five controls over the valuation process and the assumptions underlying this estimate.
 - Four of the controls that the Firm selected for testing, which it identified to address FDC assumptions, consisted of (1) the preparation and review of the annual budget, (2) management's monthly review of the consolidated financial statements, (3) a review of whether certain data were accurately entered into the application that the issuer used to value its oil and gas properties, and (4) an annual review of a reserve report prepared by a specialist. The Firm failed to ascertain whether these controls addressed the risks related to the FDC assumptions underlying the estimated cash flows used to value these assets, and it did not identify and test any other control that did so. (AS 2201.42)

- The issuer used a spreadsheet to calculate the price assumptions, which were also significant assumptions underlying the estimated cash flows. The issuer calculated the price assumptions for each type of commodity based on certain historical prices ("benchmark prices"), to which it applied adjustments for conditions specific to each oil and gas property ("differentials"). To address the price assumptions, the Firm selected for testing a fifth control, which consisted of (1) a review to determine whether the price assumptions were accurately transferred from the spreadsheet into the application that the issuer used to value its oil and gas properties and (2) an evaluation of the differentials within the spreadsheet. This control was not designed to address the reasonableness of the benchmark prices used to determine the price assumptions, and the Firm did not identify and test any other control that did so. (AS 2201.39)
- To test the reasonableness of the issuer's price assumptions and the FDCs, the Firm performed procedures in which it compared the issuer's assumptions to other amounts. These procedures were insufficient in the following respects –
 - To test the price assumptions, the Firm compared the assumptions that the issuer used to the prices that the issuer realized during the year. The Firm failed, however, to identify that there were differences that could have resulted in a material misstatement and to investigate those differences. In addition, for one identified difference, the Firm limited its procedures to inquiring of management, without obtaining corroboration of the explanations. (AS 2501.11)
 - The Firm failed to consider the drop in oil and gas prices in recent years when determining that historical amounts used in its procedures to test FDCs were relevant. (AS 2501.11)

- The issuer operated certain properties under joint-interest arrangements that required the issuer to remit a portion of the proceeds from the sale of oil and gas produced from these properties to the other interest owners. The issuer recorded its estimated share of the revenue and the related account receivable upon the sale. When the issuer received the proceeds from the sale transaction, including both its share and the other interest owner's share, the issuer recorded the entire proceeds as a reduction of its accounts receivable balance ("unapplied cash") until it determined the amount required to be remitted to the other interest owners. The issuer then reclassified this amount to joint-interest accounts payable. The Firm's testing related to unapplied cash was insufficient. Specifically –
 - The Firm failed to identify and test any controls related to the issuer's process to reclassify unapplied cash between accounts receivable and joint-interest accounts payable. (AS 2201.39)
 - The Firm failed to perform any substantive procedures to test the unapplied cash, including evaluating the effects on the financial statements of the balance sheet misclassification of the amounts to be remitted to the other interest owners. (AS 2301.08; AS 2810.30)

A.7 Issuer G

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 on the effectiveness of ICFR. For one of the issuer's segments, the issuer provided services to customers pursuant to contracts that often had multiple deliverables. The issuer recognized revenue for each contract deliverable on a performance basis that was measured using either units ("output-based") or ratably over the timeframe that services were provided. The values of the deliverables were determined using a budget spreadsheet and those values were ultimately reflected in the contracts; key information from the budget spreadsheet was entered into the issuer's revenue system. The Firm's testing related to the recognition of revenue for this segment was insufficient. Specifically –

- The Firm identified deficiencies in certain controls over the data in the budget spreadsheet. The Firm identified and tested four compensating

controls. The Firm's testing of these compensating controls was deficient, as follows –

- For one of these compensating controls, which included a review of the realization variances and backlog variances of projects outside of established ranges, the Firm failed to ascertain and evaluate the nature of the review procedures that the control owner performed in determining that certain variances outside of the established ranges did not need to be investigated. (AS 2201.68)
- The three other compensating controls consisted of reviews of the issuer's financial results. The Firm failed to evaluate whether these controls were designed to operate at a level of precision that would detect misstatements that could be material related to the determination of revenue from the deliverables. (AS 2201.68)
- The Firm failed to perform sufficient substantive procedures to test the recognition of this revenue, as follows –
 - For the revenue items selected for testing, the Firm failed to test the reasonableness of the budget for each deliverable, which was the basis for the allocation of the contractual revenue applied to the individual deliverables. Specifically, the Firm's procedures were limited to comparing the amounts recorded in the revenue system to the budget spreadsheet and to the total contract value. (AS 2301.08)
 - The Firm failed to sufficiently evaluate whether the total budgeted units, which were used to calculate the revenue recognized for individual deliverables of output-based revenue, were accurate. Specifically, the Firm's procedures were limited to comparing the total units in the revenue system to the budget spreadsheet, without determining whether the total units in each budget, and in the revenue system, agreed with the terms in the customer contracts. (AS 2301.08)

A.8 Issuer H

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

- The Firm tested information technology general controls ("ITGCs") for financially relevant applications and identified multiple deficiencies in controls over access to certain databases. Most of these control deficiencies remained unremediated as of the year end. The Firm also identified a deficiency that no controls existed over the accuracy and completeness of reports used in the operation of IT-dependent manual controls. The Firm performed procedures in order to rely on the accuracy and completeness of data used by certain automated controls and reports used in the operation of certain IT-dependent manual controls. These procedures were not sufficient in the following respects –
 - The Firm's additional procedures to evaluate whether access to certain databases had been appropriately restricted were performed based on user profiles after year end and did not provide it with evidence regarding the effectiveness of the access controls during the year. (AS 2201.46-.47)
 - The Firm's testing of the accuracy and completeness of certain of these reports was limited to testing only one transaction from only one instance of each report it selected. (AS 2201.46-.47)
 - The Firm's testing of the accuracy and completeness of certain of these reports used a benchmarking strategy, in which it relied on testing performed in a prior year; this strategy was inappropriate given that ITGC deficiencies existed in the prior year. (AS 2201.46-.47, .B29, and .B33)
- For one category of revenue, the Firm selected for testing a control that addressed whether revenue transactions had occurred. This control consisted of (1) the manual preparation, based on the control owners' review of each revenue transaction, of a schedule of differences between anticipated revenue transactions and those that had occurred and (2) the

reconciliation of this schedule to the recorded revenue. The Firm failed to sufficiently test this control, as it failed to ascertain and evaluate the procedures performed by the control owners to review the revenue transactions and prepare the schedule of differences. (AS 2201.42 and .44)

A.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 –

- During the year, the issuer acquired a significant business. The Firm's testing of the issuer's accounting for the business combination was insufficient, as follows –
 - The Firm failed to perform sufficient procedures to evaluate the reasonableness of the cash-flow forecasts that the issuer used to determine the fair value of certain acquired intangible assets. Specifically –
 - The issuer developed the cash-flow forecasts by using the actual revenue for the prior year ("the base year"), adjusted for the effects of foreign-currency exchange-rate fluctuations ("consistent-currency assumption"), and applying forecasted growth rates for each subsequent year. The Firm's procedures to evaluate the reasonableness of the base-year revenue were limited to (1) inquiring of management, (2) obtaining management's calculation of the effects of foreign-currency exchange-rate fluctuations on the prior-year revenue, and (3) inspecting movements in the exchange rates for a selection of currencies used in management's calculation. These procedures were insufficient, as the Firm failed to (1) evaluate, beyond inquiry, the appropriateness of the issuer using a consistent-currency assumption and (2) test the accuracy and completeness of the data used in management's calculation of the effects of foreign-currency exchange-rate fluctuations. (AS 2502.26, .28, and .39)

- The Firm failed to sufficiently evaluate the reasonableness of the revenue growth rates that the issuer applied in the first two years of the forecast period. Specifically, the Firm's testing of the first-year revenue growth rate was limited to inquiring of management. To test the second-year revenue growth rate, the Firm calculated a growth rate by annualizing a portion of the projected revenue for the first year and compared that calculated growth rate to those provided by external analysts; the Firm concluded the calculated growth rate was reasonable. The Firm, however, failed to identify that its calculated growth rate differed significantly from the second-year revenue growth rate that the issuer used in its forecast. (AS 2502.26 and .28)
- The issuer allocated the acquired goodwill and intangible assets to its reporting units based on financial operating results for the 12 months immediately preceding the date that it performed its annual goodwill impairment test. This date was more than seven months after the acquisition date. The financial operating results used to allocate the acquired goodwill and intangible assets were significantly lower than the projected financial operating results at the acquisition date. The Firm observed that the final allocation of goodwill and acquired intangible assets would continue to be refined during the measurement period of the business combination. The Firm failed to perform any procedures to evaluate the appropriateness of using financial results as of a date more than seven months after the acquisition (and not the information available at the time of the acquisition) to allocate goodwill and acquired intangible assets to its reporting units. (AS 2502.26, .28, and .31)
- The Firm's procedures to test the issuer's analysis of the possible impairment of certain finite-lived intangible assets for one reporting unit were insufficient. The issuer identified potential indicators of impairment related to these intangible assets and evaluated these assets for possible impairment at the reporting-unit level. In concluding that the issuer's impairment assessment was reasonable, the Firm failed to sufficiently

evaluate whether the issuer's impairment analysis was prepared using the appropriate unit of accounting, as it failed to consider evidence that suggested that identifiable and independent cash flows were available at a level lower than the reporting unit. (AS 2501.11; AS 2810.03)

A.10 Issuer J

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

- The issuer held a majority of its raw materials and finished goods inventory at one of its manufacturing facilities and performed daily cycle counts of this inventory. The Firm's procedures to test the existence, and the controls over the existence, of this inventory were insufficient. Specifically, in testing whether the cycle-count procedures that the issuer used for this inventory were sufficiently reliable, the Firm failed to consider the frequency of the counts and the aggregate deviations identified in the counts. (AS 2201.42 and .44; AS 2510.11)
- The Firm failed to perform sufficient procedures related to the valuation of inventory, as follows –
 - The Firm selected for testing a control that consisted of management's quarterly analysis and review of overhead and purchase-price manufacturing variances capitalized to inventory. The Firm's testing of the review aspect of this control was insufficient. Specifically, the Firm failed to ascertain and evaluate the nature of the review procedures performed by the control owners, including the criteria used to identify items for follow up and how those items were resolved. (AS 2201.42 and .44)
 - The Firm's substantive procedures to test overhead costs subject to capitalization were insufficient. Specifically –
 - To test the capitalized overhead costs, the Firm obtained the issuer's reconciliation of the gross margin based on standard

costing to the recorded gross margin. The Firm's procedures to test this reconciliation were limited to (1) testing the mathematical accuracy of the calculations of the standard and recorded gross margins used in the reconciliation, (2) comparing the balances included in the reconciliation to the general ledger, and (3) inspecting the reconciliation for unusual variances as compared to the prior year. The Firm, however, failed to test the accuracy of the amounts included in the reconciliation. (AS 2301.08)

- The Firm failed to sufficiently test the allocation of the components of overhead costs among the categories of ending inventory. Specifically, the Firm limited its testing to comparing the standard overhead rates for a sample of items to bills-of-materials or other documents prepared by the issuer. The Firm, however, failed to test the accuracy and completeness of the overhead costs included in these documents. (AS 1105.10)

A.11 Issuer K

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 on the effectiveness of ICFR –

- The Firm identified long-term investments as a significant account and valuation as a relevant assertion; however, it failed to identify and test any controls over the valuation of long-term investments. (AS 2201.39)
- The issuer used a model, which used cash-flow forecasts as significant inputs, to determine the fair value of long-term investments. The Firm's testing of the fair value of long-term investments was not sufficient, as it failed to perform any procedures to evaluate the reasonableness of the cash-flow forecasts that the issuer used in determining the fair value. (AS 2502.26 and .28)

B. Auditing Standards

Each deficiency described in Part I.A above could relate to several provisions of the standards that govern the conduct of audits. The paragraphs of the standards that are cited for each deficiency are those that most directly relate to the deficiency. The deficiencies also may relate, however, to other paragraphs of those standards and to other auditing standards, including those concerning due professional care, responses to risk assessments, and audit evidence.

Many audit deficiencies involve a lack of due professional care. Paragraphs .02, .05, and .06 of AS 1015, *Due Professional Care in the Performance of Work*, require the independent auditor to plan and perform his or her work with due professional care and set forth aspects of that requirement. AS 1015.07-.09, and paragraph .07 of AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*, specify that due professional care requires the exercise of professional skepticism. These standards state that professional skepticism is an attitude that includes a questioning mind and a critical assessment of the appropriateness and sufficiency of audit evidence.

AS 2301.03, .05, and .08 require the auditor to design and implement audit responses that address the risks of material misstatement. Paragraph .04 of AS 1105, *Audit Evidence*, requires the auditor to plan and perform audit procedures to obtain sufficient appropriate audit evidence to provide a reasonable basis for the audit opinion. Sufficiency is the measure of the quantity of audit evidence, and the quantity needed is affected by the risk of material misstatement (in the audit of financial statements) or the risk associated with the control (in the audit of ICFR) and the quality of the audit evidence obtained. The appropriateness of evidence is measured by its quality; to be appropriate, evidence must be both relevant and reliable in providing support for the related conclusions.

The paragraphs of the standards that are described immediately above are not cited in Part I.A, unless those paragraphs are the most directly related to the relevant deficiency.

B.1. List of Specific Auditing Standards Referenced in Part I.A

The table below lists the specific auditing standards that are referenced in Part I.A of this report, cross-referenced to the issuer audits for which each standard is cited. For each auditing standard, the table also provides the number of distinct deficiencies

for which the standard is cited for each of the relevant issuer audits. This information identifies only the number of times that the standard is referenced, regardless of whether the reference includes multiple paragraphs or relates to multiple financial statement accounts.

PCAOB Auditing Standards	Audits	Number of Deficiencies per Audit
AS 1105, <i>Audit Evidence</i>	Issuer D	2
	Issuer J	1
AS 1210, <i>Using the Work of a Specialist</i>	Issuer C	1
AS 2201, <i>An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements</i>	Issuer A	5
	Issuer B	5
	Issuer C	2
	Issuer E	1
	Issuer F	3
	Issuer G	2
	Issuer H	4
	Issuer J	2
	Issuer K	1
AS 2301, <i>The Auditor's Responses to the Risks of Material Misstatement</i>	Issuer D	6
	Issuer F	1
	Issuer G	2
	Issuer J	1
AS 2501, <i>Auditing Accounting Estimates</i>	Issuer A	2
	Issuer B	2
	Issuer E	3
	Issuer F	2
	Issuer I	1
AS 2502, <i>Auditing Fair Value Measurements and Disclosures</i>	Issuer A	2
	Issuer B	4

PCAOB Auditing Standards	Audits	Number of Deficiencies per Audit
AS 2502, Auditing Fair Value Measurements and Disclosures - continued	Issuer C	1
	Issuer I	3
	Issuer K	1
AS 2510, Auditing Inventories	Issuer B	2
	Issuer D	2
	Issuer J	1
AS 2810, Evaluating Audit Results	Issuer B	4
	Issuer F	1
	Issuer I	1

B.2. Financial Statement Accounts or Auditing Areas Related to Identified Audit Deficiencies

The table below lists the financial statement accounts or auditing areas related to the deficiencies included in Part I.A of this report and identifies the audits described in Part I.A where deficiencies relating to the respective areas were observed.

	AS 1105	AS 1210	AS 2201	AS 2301	AS 2315	AS 2501	AS 2502	AS 2510	AS 2810
Business Combinations			A				A, I		
Fixed Assets		C	C, E, F			E, F	C		
Impairment of goodwill and intangible assets			B			I	B		B, I
Information Technology			H						
Inventory and related reserves	D, J		B, J	D, J		B		B, D, J	
Investment securities,			C, K				K		

	AS 1105	AS 1210	AS 2201	AS 2301	AS 2315	AS 2501	AS 2502	AS 2510	AS 2810
including derivatives									
Revenue, including accounts receivable, deferred revenue, and allowance	D		A, B, F, G, H	D, F, G		A, B			F

B.3. Audit Deficiencies by Industry

The table below lists the industries⁴ of the issuers for which audit deficiencies were discussed in Part I.A of this report and cross references the issuers to the specific auditing standards related to the deficiencies.⁵

	AS 1105	AS 1210	AS 2201	AS 2301	AS 2501	AS 2502	AS 2510	AS 2810
Consumer Discretionary			H					
Energy			E, F	F	E, F			F
Health Care			G	G				
Industrials	D		B, K	D	B	B, K	B	B
Information Technology	J		A, J	J	A	A	J	
Materials					I	I		I
Utilities		C	C			C		

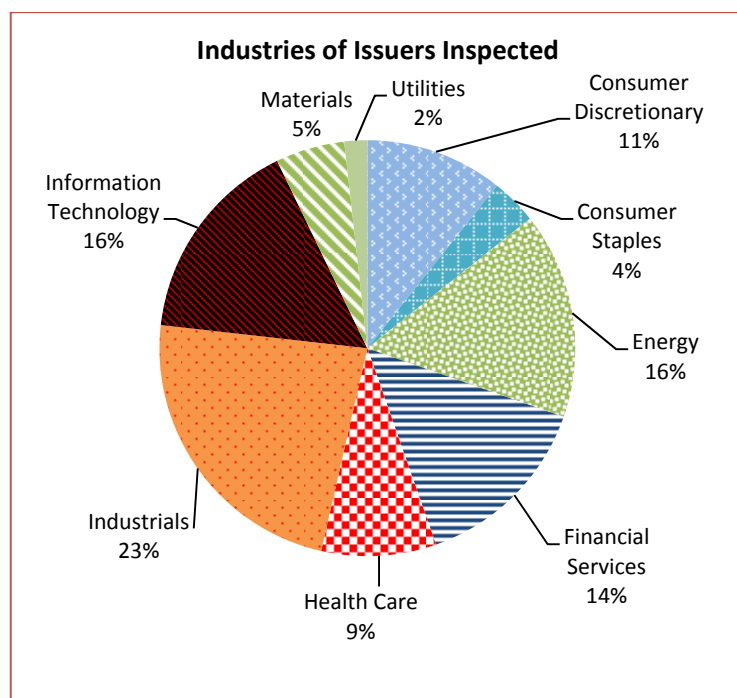
⁴ The majority of industry sector data is based on Global Industry Classification Standard ("GICS") data obtained from Standard & Poor's ("S&P"). In instances where GICS for an issuer is not available from S&P, classifications are assigned based upon North American Industry Classification System data.

⁵ Where identifying the industry of the issuer may enhance the understanding of the description of a deficiency in Part I.A, industry information is also provided there, unless doing so would have the effect of making the issuer identifiable.

C. Data Related to the Issuer Audits Selected for Inspection⁶

C.1. Industries of Issuers Inspected

The chart below categorizes the 56 issuers whose audits were inspected in 2016, based on the issuer's industry.⁷



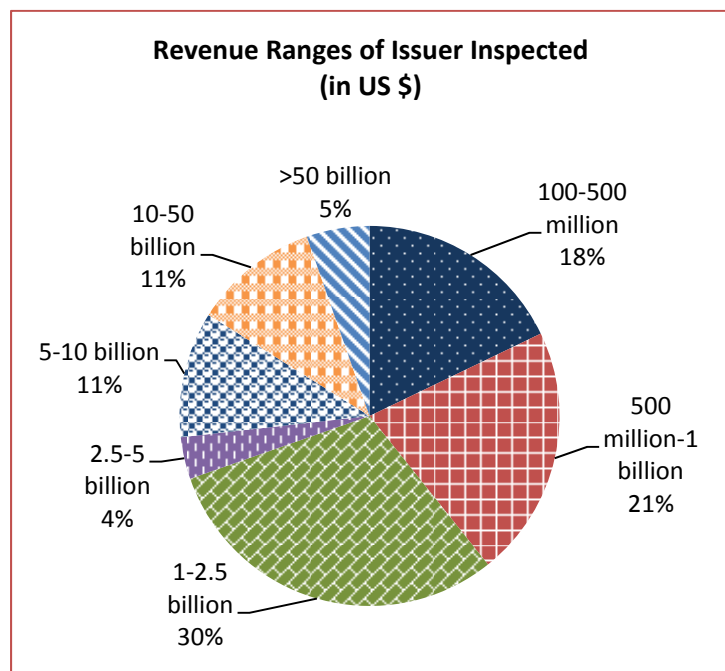
Industry	Number of Audits Inspected	Percentage
Consumer Discretionary	6	11%
Consumer Staples	2	4%
Energy	9	16%
Financial Services	8	14%
Health Care	5	9%
Industrials	13	23%
Information Technology	9	16%
Materials	3	5%
Utilities	1	2%

⁶ Where the audit work inspected related to an engagement in which the Firm played a role but was not the principal auditor, the industry and the revenue included in the tables and charts in this section are those of the entity for which an audit report was issued by the primary auditor. As discussed above, the inspection process included reviews of portions of 53 selected issuer audits completed by the Firm and the Firm's audit work on three other issuer audit engagements in which it played a role but was not the principal auditor.

⁷ See Footnote 4 for additional information on how industry sectors were classified.

C.2. Revenue Ranges of Issuers Inspected

The chart below categorizes, based upon revenue, the 56 issuers whose audits were inspected in 2016.⁸ This presentation of revenue data is intended to provide information about the size of issuer audits that were inspected and is not indicative of whether the inspection included a review of the Firm's auditing of revenue in the issuer audits selected for review.



Revenue (in US\$)	Number of Audits inspected	Percentage
100-500 million	10	18%
500 million-1 billion	12	21%
1-2.5 billion	17	30%
2.5-5 billion	2	4%
5-10 billion	6	11%
10-50 billion	6	11%
>50 billion	3	5%

⁸ The revenue amounts reflected in the chart are for the issuer's fiscal year end that corresponds to the audit inspected by the PCAOB. The revenue amounts were obtained from S&P and reflect a standardized approach to presenting revenue amounts.

D. Information Concerning PCAOB Inspections that is Generally Applicable to Annually Inspected Firms

Board inspections include reviews of certain portions of selected audit work performed by the inspected firm and reviews of certain aspects of the firm's quality control system. The inspections are designed to identify deficiencies in audit work and defects or potential defects in the firm's system of quality control related to the firm's audits. The focus on deficiencies, defects, and potential defects 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. Further, the inclusion in an inspection report of certain deficiencies, defects, and potential defects should not be construed as an indication that the Board has made any determination about other aspects of the inspected firm's systems, policies, procedures, practices, or conduct not included within the report.

D.1. Reviews of Audit Work

Inspections include reviews of portions of selected audits of financial statements and, where applicable, audits of ICFR. The inspection team selects the audits, and the specific portions of those audits, that it will review, and the inspected firm is not allowed an opportunity to limit or influence the selections. For each specific portion of the audit that is selected, the inspection team reviews the engagement team's work papers and interviews engagement personnel regarding those portions. If the inspection team identifies a potential issue that it is unable to resolve through discussion with the firm and any review of additional work papers or other documentation, the inspection team ordinarily provides the firm with a written comment form on the matter and the firm is allowed the opportunity to provide a written response to the comment form. If the response does not resolve the inspection team's concerns, the matter is considered a deficiency and is evaluated for inclusion in the inspection report. Identified deficiencies

in the audit work that exceed a significance threshold (which is described in Part I.A of the inspection report) are summarized in the public portion of the inspection report.⁹

Audit deficiencies that the inspection team may identify include a firm's failure to identify, or to address appropriately, financial statement misstatements, including failures to comply with disclosure requirements,¹⁰ as well as a firm's failure to perform, or to perform sufficiently, certain necessary tests of controls and substantive audit procedures. An inspection of an annually inspected firm does not involve the review of all of the firm's audits, nor is it designed to identify every deficiency in the reviewed audits. Accordingly, a Board inspection report should not be understood to provide any assurance that a firm's audit work, or the relevant issuers' financial statements or reporting on ICFR, are free of any deficiencies not specifically described in an inspection report.

In reaching its conclusions about whether a deficiency exists, an inspection team considers whether audit documentation or any other evidence that a firm might provide to the inspection team supports the firm's contention that it performed a procedure,

⁹ 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. In addition, 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 for purposes of imposing legal liability.

¹⁰ 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 the applicable financial reporting framework, the Board's practice is to report that information to the Securities and Exchange Commission ("SEC" or "the Commission"), which has jurisdiction to determine proper accounting in issuers' financial statements. Any description in this report of financial statement misstatements or failures to comply with SEC disclosure requirements should not be understood as an indication that the SEC has considered or made any determination regarding these issues unless otherwise expressly stated.

obtained evidence, or reached an appropriate conclusion. In some cases, the conclusion that a firm did not perform a procedure may be based on the absence of documentation and the absence of persuasive other evidence, even if the firm claimed to have performed the procedure. AS 1215, *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. In the case of every matter cited in the public portion of a final inspection report, the inspection team has carefully considered any contention by the firm that it did so but just did not document its work, and the inspection team has concluded that the available evidence does not support the contention that the firm sufficiently performed the necessary work.

The Board cautions against extrapolating from the results presented in the public portion of a report to broader conclusions about the frequency of deficiencies throughout the firm's practice. Individual audits and areas of inspection focus are most often selected on a risk-weighted basis and not randomly. Areas of focus vary among selected audits, but often involve audit work on the most difficult or inherently uncertain areas of financial statements. Thus, the audit work is generally selected for inspection based on 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.

D.2. Review of a Firm's Quality Control System

QC 20, *System of Quality Control for a CPA Firm's Accounting and Auditing Practice*, provides that an auditing firm has a responsibility to ensure that its personnel comply with the applicable professional standards. This standard specifies that a firm's system of quality control should encompass the following elements: (1) independence, integrity, and objectivity; (2) personnel management; (3) acceptance and continuance of issuer audit engagements; (4) engagement performance; and (5) monitoring.

The inspection team's assessment of a firm's quality control system is derived both from the results of its procedures specifically focused on the firm's quality control policies and procedures, and also from inferences that can be drawn from deficiencies in the performance of individual audits. Audit deficiencies, whether alone or when

aggregated, may indicate areas where a firm's system has failed to provide reasonable assurance of quality in the performance of audits. Even deficiencies that do not result in an insufficiently supported audit opinion or a failure to obtain sufficient appropriate audit evidence to fulfill the objectives of the firm's role in an audit may indicate a defect or potential defect in a firm's quality control system.¹¹ If identified deficiencies, when accumulated and evaluated, indicate defects or potential defects in the firm's system of quality control, the nonpublic portion of this report would include a discussion of those issues. When evaluating whether identified deficiencies in individual audits indicate a defect or potential defect in a firm's system of quality control, the inspection team considers the nature, significance, and frequency of deficiencies;¹² related firm methodology, guidance, and practices; and possible root causes.

Inspections also include a review of certain of the firm's practices, policies, and processes related to audit quality, which constitute a part of the firm's quality control system. The inspection team customizes the procedures it performs with respect to the firm's practices, policies, and processes related to audit quality, bearing in mind the firm's structure, procedures performed in prior inspections, past and current inspection observations, an assessment of risk related to each area, and other factors. The areas generally considered for review include (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 issuer audit engagements, 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 audits; and

¹¹ Not every audit deficiency suggests a defect or potential defect in a firm's quality control system, and this report does not discuss every audit deficiency the inspection team identified.

¹² An evaluation of the frequency of a type of deficiency may include consideration of how often the inspection team reviewed audit work that presented the opportunity for similar deficiencies to occur. In some cases, even a type of deficiency that is observed infrequently in a particular inspection may, because of some combination of its nature, its significance, and the frequency with which it has been observed in previous inspections of the firm, be cause for concern about a quality control defect or potential defect.

(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 defects or potential defects in quality control. A description of the procedures generally applied to these areas is below.

D.2.a. Review of Management Structure and Processes, Including the Tone at the Top

Procedures in this area are designed to focus on (1) how management is structured and operates the firm's business, and the implications that the management structure and processes have on audit performance and (2) whether actions and communications by the firm's leadership – the tone at the top – demonstrate a commitment to audit quality. To assess this area, the inspection team may interview members of the firm's leadership and review significant management reports, communications, and documents, as well as information regarding financial metrics and other processes that the firm uses to plan and evaluate its business.

D.2.b. Review of Practices for Partner Management, Including Allocation of Partner Resources and Partner Evaluation, Compensation, Admission, and Disciplinary Actions

Procedures in this area are designed to focus on (1) 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 distinct from marketing or other activities of the firm; (2) the firm's processes for allocating its partner resources; and (3) the accountability and responsibilities of the different levels of firm management with respect to partner management. The inspection team may interview members of the firm's management and review documentation related to certain of these topics. In addition, the inspection team's evaluation may include the results of interviews of audit partners regarding their responsibilities and allocation of time. Further, the inspection team may review a sample of partners' personnel files.

D.2.c. Review of Policies and Procedures for Considering and Addressing the Risks Involved in Accepting and Retaining Issuer Audit Engagements, Including the Application of the Firm's Risk-Rating System

The inspection team may consider the firm's documented policies and procedures in this area. In addition, the inspection team may select certain issuer audits to (1) evaluate compliance with the firm's policies and procedures for identifying and assessing the risks involved in accepting or continuing the issuer audit engagements and (2) observe whether the audit procedures were responsive to the risks of material misstatement identified during the firm's process.

D.2.d. Review of Processes Related to a Firm's Use of Audit Work that the Firm's Foreign Affiliates Perform on the Foreign Operations of the Firm's U.S. Issuer Audits

The inspection team may review the firm's policies and procedures related to its supervision and control of work performed by foreign affiliates on the firm's U.S. issuer audits, review available information relating to the most recent internal inspections of foreign affiliated firms, interview members of the firm's leadership, and review the U.S. engagement teams' supervision concerning, and procedures for control of, the audit work that the firm's foreign affiliates performed on a sample of audits.

D.2.e. Review of a 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 Defects or Potential Defects in Quality Control

D.2.e.i. Review of Processes for Identifying and Assessing Indicators of Deficiencies in Audit Performance

Procedures in this area are 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 may interview members of the firm's management and review documents relating to the firm's identification and evaluation

of, and response to, possible indicators of deficiencies in audit performance. In addition, the inspection team may review documents related to the design, operation, and evaluation of findings of the firm's internal inspection program, and may compare the results of its review of audit work to those from the internal inspection's review of the same audit work.

D.2.e.ii. Review of Response to Defects or Potential Defects in Quality Control

The inspection team may review steps the firm has taken to address possible quality control deficiencies and assess the design and effectiveness of the underlying processes. In addition, the inspection team may inspect audits of issuers whose audits had been reviewed during previous PCAOB inspections of the firm to ascertain whether the audit procedures in areas with previous deficiencies have improved.

D.2.e.iii. Review of Certain Other Policies and Procedures Related to Monitoring Audit Quality

The inspection team may assess policies, procedures, and guidance related to aspects of independence requirements and the firm's consultation processes, as well as the firm's compliance with these requirements and processes. In addition, the inspection team may review documents, including certain newly issued policies and procedures, and interview firm management to consider the firm's methods for developing audit policies, procedures, and methodologies, including internal guidance and training materials.

END OF PART I

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

APPENDIX B

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.¹³

¹³ The Board does not make public any of a firm's comments that address a nonpublic portion of the report unless a firm specifically requests otherwise. In some cases, the result may be that none of a firm's response is made publicly available. 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.



November 1, 2017

Ms. Helen A. Munter, Director
Division of Registration and Inspections
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006

Re: Response to Draft Report on the 2016 Inspection of PricewaterhouseCoopers LLP

Dear Ms. Munter:

On behalf of PricewaterhouseCoopers LLP (the "Firm"), we are pleased to provide our response to the Public Company Accounting Oversight Board's ("PCAOB" or the "Board") Draft Report on the 2016 Inspection of our Firm's 2015 audits (the "Report").

We recognize the inspection process provides a valuable opportunity to improve the quality of our audits. We continue to support the PCAOB in its mission and are committed to furthering the public interest through the preparation of informative, accurate and independent audit reports. Bringing value to the capital markets by consistently performing high-quality audits remains our top priority, and we will address the matters raised in the Report in a thorough and thoughtful way. We appreciate that many of our stakeholders will review the PCAOB's final report and our response and have therefore included a link to our 2017 audit quality report to encourage our stakeholders to see the tangible steps we are taking to maintain and improve audit quality.

<http://www.pwc.com/us/auditquality>

We have evaluated each of the observations set forth in *Part I - Inspection Procedures and Certain Observations* of the Report and have taken appropriate actions under both PCAOB standards and our policies. Our evaluation included those steps we considered necessary to comply with AS 2901, *Consideration of Omitted Procedures After the Report Date*, and where applicable, AS 2905, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report* and AS No. 2201, *An Audit of Internal Control Over Financial Reporting That Is Integrated With An Audit of Financial Statements*.

We look forward to continuing our dialogue with the PCAOB and would be pleased to discuss any aspect of this response or any other questions you may have.

Sincerely,

A handwritten signature in black ink that reads "Tim Ryan".

Tim Ryan
US Chairman and Senior Partner
PricewaterhouseCoopers LLP

A handwritten signature in black ink that reads "Maria C. Moats".

Maria C. Moats
US Assurance Leader
PricewaterhouseCoopers LLP

APPENDIX C

AUDITING STANDARDS REFERENCED IN PART I

This appendix provides the text of the auditing standard paragraphs that are referenced in Part I.A of this report. Footnotes that are included in this appendix, and any other Notes, are from the original auditing standards that are referenced. While this appendix contains the specific portions of the relevant standards cited with respect to the deficiencies in Part I.A of this report, other portions of the standards (including those described in Part I.B of this report) may provide additional context, descriptions, related requirements, or explanations; the complete standards are available on the PCAOB's website at <http://pcaobus.org/STANDARDS/Pages/default.aspx>.

AS 1105, Audit Evidence		
SUFFICIENT APPROPRIATE AUDIT EVIDENCE		
Using Information Produced by the Company		
AS 1105.10	<p>When using 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:³</p> <ul style="list-style-type: none"> ▪ Test the accuracy and completeness of the information, or test the controls over the accuracy and completeness of that information; and ▪ Evaluate whether the information is sufficiently precise and detailed for purposes of the audit. 	Issuers D and J
<p><u>Footnote to AS 1105.10</u></p> <p>³ When using the work of a specialist engaged or employed by management, see AS 1210, <i>Using the Work of a Specialist</i>. When using information produced by a service organization or a service auditor's report as audit evidence, see AS 2601, <i>Consideration of an Entity's Use of a Service Organization</i>, and for integrated audits, see AS 2201, <i>An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements</i>.</p>		

AS 1210, Using the Work of a Specialist		
USING THE FINDINGS OF THE SPECIALIST		
AS 1210.12	<p>The appropriateness and reasonableness of methods and assumptions used and their application are the responsibility of the specialist. The auditor should (a) obtain an understanding of the methods and assumptions used by the specialist, (b) make appropriate tests of data provided to the specialist, taking into account the auditor's assessment of control risk, and (c) evaluate whether the specialist's findings support the related assertions in the financial statements. Ordinarily, the auditor would use the work of the specialist unless the auditor's procedures lead him or her to believe the findings are unreasonable in the circumstances. If the auditor believes the findings are unreasonable, he or she should apply additional procedures, which may include obtaining the opinion of another specialist.</p>	Issuer C

AS 2201, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements		
Selecting Controls to Test		
AS 2201.39	<p>The auditor should test those controls that are important to the auditor's conclusion about whether the company's controls sufficiently address the assessed risk of misstatement to each relevant assertion.</p>	Issuers A, B, C, F, and K
TESTING CONTROLS		
Testing Design Effectiveness		
AS 2201.42	<p>The auditor should test the design effectiveness of controls by determining whether the company's controls, if they are operated as prescribed by persons possessing the necessary authority and competence to perform the control effectively, satisfy the company's control objectives and can effectively prevent or detect errors or fraud that could result in material misstatements in the financial statements.</p> <p>Note: A smaller, less complex company might achieve its control objectives in a different manner from a larger, more complex organization. For example, a smaller, less complex company might have fewer employees in the accounting function, limiting opportunities to segregate duties and</p>	Issuers A, C, E, F, H, and J

AS 2201, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements		
	<p>leading the company to implement alternative controls to achieve its control objectives. In such circumstances, the auditor should evaluate whether those alternative controls are effective.</p>	
Testing Operating Effectiveness		
AS 2201.44	<p>The auditor should test the operating effectiveness of a control by determining whether the control is operating as designed and whether the person performing the control possesses the necessary authority and competence to perform the control effectively.</p> <p>Note: In some situations, particularly in smaller companies, a company might use a third party to provide assistance with certain financial reporting functions. When assessing the competence of personnel responsible for a company's financial reporting and associated controls, the auditor may take into account the combined competence of company personnel and other parties that assist with functions related to financial reporting.</p>	Issuers A, B, C, E, H, and J
Relationship of Risk to the Evidence to be Obtained		
AS 2201.46	<p>For each control selected for testing, the evidence necessary to persuade the auditor that the control is effective depends upon the risk associated with the control. The risk associated with a control consists of the risk that the control might not be effective and, if not effective, the risk that a material weakness would result. As the risk associated with the control being tested increases, the evidence that the auditor should obtain also increases</p> <p>Note: Although the auditor must obtain evidence about the effectiveness of controls for each relevant assertion, the auditor is not responsible for obtaining sufficient evidence to support an opinion about the effectiveness of each individual control. Rather, the auditor's objective is to express an opinion on the company's internal control over financial reporting overall. This allows the auditor to vary the evidence obtained regarding the effectiveness of individual controls selected for</p>	Issuer H

AS 2201, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements

	testing based on the risk associated with the individual control.	
AS 2201.47	<p>Factors that affect the risk associated with a control include –</p> <ul style="list-style-type: none"> ▪ The nature and materiality of misstatements that the control is intended to prevent or detect; ▪ The inherent risk associated with the related account(s) and assertion(s); ▪ Whether there have been changes in the volume or nature of transactions that might adversely affect control design or operating effectiveness; ▪ Whether the account has a history of errors; ▪ The effectiveness of entity-level controls, especially controls that monitor other controls; ▪ The nature of the control and the frequency with which it operates; ▪ The degree to which the control relies on the effectiveness of other controls (<i>e.g.</i>, the control environment or information technology general controls); ▪ The competence of the personnel who perform the control or monitor its performance and whether there have been changes in key personnel who perform the control or monitor its performance; ▪ Whether the control relies on performance by an individual or is automated (<i>i.e.</i>, an automated control would generally be expected to be lower risk if relevant information technology general controls are effective); and <p>Note: A less complex company or business unit with simple business processes and centralized accounting operations might have relatively simple information systems that make greater use of off-the-shelf packaged software without modification. In the areas in which off-the-shelf software is used, the auditor's testing of information technology controls might focus on the application controls built into the pre-</p>	Issuer H

AS 2201, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements		
	<p>packaged software that management relies on to achieve its control objectives and the IT general controls that are important to the effective operation of those application controls.</p> <ul style="list-style-type: none"> ▪ The complexity of the control and the significance of the judgments that must be made in connection with its operation. <p>Note: Generally, a conclusion that a control is not operating effectively can be supported by less evidence than is necessary to support a conclusion that a control is operating effectively.</p>	
EVALUATING IDENTIFIED DEFICIENCIES		
AS 2201.68	<p>The auditor should evaluate the effect of compensating controls when determining whether a control deficiency or combination of deficiencies is a material weakness. To have a mitigating effect, the compensating control should operate at a level of precision that would prevent or detect a misstatement that could be material.</p>	Issuer G
APPENDIX B - Special Topics		
BENCHMARKING OF AUTOMATED CONTROLS		
AS 2201.B29	<p>If general controls over program changes, access to programs, and computer operations are effective and continue to be tested, and if the auditor verifies that the automated application control has not changed since the auditor established a baseline (<i>i.e.</i>, last tested the application control), the auditor may conclude that the automated application control continues to be effective without repeating the prior year's specific tests of the operation of the automated application control. The nature and extent of the evidence that the auditor should obtain to verify that the control has not changed may vary depending on the circumstances, including depending on the strength of the company's program change controls.</p>	Issuer H
AS 2201.B33	<p>After a period of time, the length of which depends upon the circumstances, the baseline of the operation of an</p>	Issuer H

AS 2201, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements		
	<p>automated application control should be reestablished. To determine when to reestablish a baseline, the auditor should evaluate the following factors -</p> <ul style="list-style-type: none"> ▪ The effectiveness of the IT control environment, including controls over application and system software acquisition and maintenance, access controls and computer operations. ▪ The auditor's understanding of the nature of changes, if any, on the specific programs that contain the controls. ▪ The nature and timing of other related tests. ▪ The consequences of errors associated with the application control that was benchmarked. ▪ Whether the control is sensitive to other business factors that may have changed. For example, an automated control may have been designed with the assumption that only positive amounts will exist in a file. Such a control would no longer be effective if negative amounts (credits) begin to be posted to the account. 	

AS 2301, The Auditor's Responses to the Risks of Material Misstatement		
RESPONSES INVOLVING THE NATURE, TIMING, AND EXTENT OF AUDIT PROCEDURES		
AS 2301.08	The auditor should design and perform audit procedures in a manner that addresses the assessed risks of material misstatement for each relevant assertion of each significant account and disclosure.	Issuers D, F, G, and J
Testing Design Effectiveness		
AS 2301.19	The auditor should test the design effectiveness of the controls selected for testing by determining whether the company's controls, if they are operated as prescribed by persons possessing the necessary authority and competence to perform the control effectively, satisfy the company's control objectives and can effectively prevent or detect error or fraud that could result in material	Issuer D

AS 2301, The Auditor's Responses to the Risks of Material Misstatement		
	<p>misstatements in the financial statements.</p> <p>Note: A smaller, less complex company might achieve its control objectives in a different manner from a larger, more complex organization. For example, a smaller, less complex company might have fewer employees in the accounting function, limiting opportunities to segregate duties and leading the company to implement alternative controls to achieve its control objectives. In such circumstances, the auditor should evaluate whether those alternative controls are effective.</p>	
Testing Operating Effectiveness		
AS 2301.21	The auditor should test the operating effectiveness of a control selected for testing by determining whether the control is operating as designed and whether the person performing the control possesses the necessary authority and competence to perform the control effectively.	Issuer D
Assessing Control Risk		
AS 2301.32	The auditor should assess control risk for relevant assertions by evaluating the evidence obtained from all sources, including the auditor's testing of controls for the audit of internal control and the audit of financial statements, misstatements detected during the financial statement audit, and any identified control deficiencies.	Issuer D
SUBSTANTIVE PROCEDURES		
AS 2301.37	As the assessed risk of material misstatement increases, the evidence from substantive procedures that the auditor should obtain also increases. The evidence provided by the auditor's substantive procedures depends upon the mix of the nature, timing, and extent of those procedures. Further, for an individual assertion, different combinations of the nature, timing, and extent of testing might provide sufficient appropriate evidence to respond to the assessed risk of material misstatement.	Issuer D

AS 2301, The Auditor's Responses to the Risks of Material Misstatement		
Extent of Substantive Procedures		
AS 2301.42	The more extensively a substantive procedure is performed, the greater the evidence obtained from the procedure. The necessary extent of a substantive audit procedure depends on the materiality of the account or disclosure, the assessed risk of material misstatement, and the necessary degree of assurance from the procedure. However, increasing the extent of an audit procedure cannot adequately address an assessed risk of material misstatement unless the evidence to be obtained from the procedure is reliable and relevant.	Issuer D

AS 2501, Auditing Accounting Estimates		
EVALUATING REASONABLENESS		
AS 2501.11	<p>Review and test management's process. In many situations, the auditor assesses the reasonableness of an accounting estimate by performing procedures to test the process used by management to make the estimate. The following are procedures the auditor may consider performing when using this approach:</p> <ol style="list-style-type: none"> a. Identify whether there are controls over the preparation of accounting estimates and supporting data that may be useful in the evaluation. b. Identify the sources of data and factors that management used in forming the assumptions, and consider whether such data and factors are relevant, reliable, and sufficient for the purpose based on information gathered in other audit tests. c. Consider whether there are additional key factors or alternative assumptions about the factors. d. Evaluate whether the assumptions are consistent with each other, the supporting data, relevant historical data, and industry data. e. Analyze historical data used in developing the assumptions to assess whether the data is comparable and consistent with data of the period under audit, and consider whether such data is sufficiently reliable for the purpose. 	Issuers A, B, E, F, and I

AS 2501, Auditing Accounting Estimates		
	<p>f. Consider whether changes in the business or industry may cause other factors to become significant to the assumptions.</p> <p>g. Review available documentation of the assumptions used in developing the accounting estimates and inquire about any other plans, goals, and objectives of the entity, as well as consider their relationship to the assumptions.</p> <p>h. Consider using the work of a specialist regarding certain assumptions (AS 1210, <i>Using the Work of a Specialist</i>).</p> <p>i. Test the calculations used by management to translate the assumptions and key factors into the accounting estimate.</p>	
AS 2501.12	<p><i>Develop an expectation.</i> Based on the auditor's understanding of the facts and circumstances, he may independently develop an expectation as to the estimate by using other key factors or alternative assumptions about those factors.</p>	Issuer B

AS 2502, Auditing Fair Value Measurements and Disclosures		
Testing Management's Significant Assumptions, the Valuation Model, and the Underlying Data		
AS 2502.26	<p>The auditor's understanding of the reliability of the process used by management to determine fair value is an important element in support of the resulting amounts and therefore affects the nature, timing, and extent of audit procedures. When testing the entity's fair value measurements and disclosures, the auditor evaluates whether:</p> <p>a. Management's assumptions are reasonable and reflect, or are not inconsistent with, market information (see paragraph .06).</p> <p>b. The fair value measurement was determined using an appropriate model, if applicable.</p> <p>c. Management used relevant information that was reasonably available at the time.</p>	Issuers A, B, C, I, and K

AS 2502, Auditing Fair Value Measurements and Disclosures		
AS 2502.28	Where applicable, the auditor should evaluate whether the significant assumptions used by management in measuring fair value, taken individually and as a whole, provide a reasonable basis for the fair value measurements and disclosures in the entity's financial statements.	Issuers A, B, C, I, and K
AS 2502.31	Assumptions ordinarily are supported by differing types of evidence from internal and external sources that provide objective support for the assumptions used. The auditor evaluates the source and reliability of evidence supporting management's assumptions, including consideration of the assumptions in light of historical and market information.	Issuers A, B, and I
AS 2502.36	<p>To be reasonable, the assumptions on which the fair value measurements are based (for example, the discount rate used in calculating the present value of future cash flows),⁵ individually and taken as a whole, need to be realistic and consistent with:</p> <ul style="list-style-type: none"> a. The general economic environment, the economic environment of the specific industry, and the entity's economic circumstances; b. Existing market information; c. The plans of the entity, including what management expects will be the outcome of specific objectives and strategies; d. Assumptions made in prior periods, if appropriate; e. Past experience of, or previous conditions experienced by, the entity to the extent currently applicable; f. Other matters relating to the financial statements, for example, assumptions used by management in accounting estimates for financial statement accounts other than those relating to fair value measurements and disclosures; and g. The risk associated with cash flows, if applicable, including the potential variability in the amount and timing of the cash flows and the related effect on the discount rate. <p>Where assumptions are reflective of management's intent and ability to carry out specific courses of action, the auditor considers whether they are consistent with the entity's plans and past experience.</p>	Issuers A, B, and C

AS 2502, Auditing Fair Value Measurements and Disclosures		
<u>Footnote to AS 2502.36</u>		
<p>⁵ The auditor also should consider requirements of GAAP that may influence the selection of assumptions (see FASB Concepts Statement No. 7).</p>		
AS 2502.39	<p>The auditor should test the data used to develop the fair value measurements and disclosures and evaluate whether the fair value measurements have been properly determined from such data and management's assumptions. Specifically, the auditor evaluates whether the data on which the fair value measurements are based, including the data used in the work of a specialist, is accurate, complete, and relevant; and whether fair value measurements have been properly determined using such data and management's assumptions. The auditor's tests also may include, for example, procedures such as verifying the source of the data, mathematical recomputation of inputs, and reviewing of information for internal consistency, including whether such information is consistent with management's intent and ability to carry out specific courses of action discussed in paragraph .17.</p>	Issuer I

AS 2510, Auditing Inventories		
INVENTORIES		
AS 2510.11	<p>In recent years, some companies have developed inventory controls or methods of determining inventories, including statistical sampling, which are highly effective in determining inventory quantities and which are sufficiently reliable to make unnecessary an annual physical count of each item of inventory. In such circumstances, the independent auditor must satisfy himself that the client's procedures or methods are sufficiently reliable to produce results substantially the same as those which would be obtained by a count of all items each year. The auditor must be present to observe such counts as he deems necessary and must satisfy himself as to the effectiveness of the counting procedures used. If statistical sampling methods are used by the client in the taking of the physical inventory, the auditor must be satisfied that the sampling plan is reasonable and statistically valid, that it has been properly applied, and that the results are reasonable in the</p>	Issuers B, D, and J

AS 2510, Auditing Inventories		
	circumstances.	

AS 2810, Evaluating Audit Results		
EVALUATING THE RESULTS OF THE AUDIT OF FINANCIAL STATEMENTS		
AS 2810.03	In forming an opinion on whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework, the auditor should take into account all relevant audit evidence, regardless of whether it appears to corroborate or to contradict the assertions in the financial statements.	Issuers B and I
Evaluating the Presentation of the Financial Statements, Including the Disclosures		
AS 2810.30	<p>The auditor must evaluate whether the financial statements are presented fairly, in all material respects, in conformity with the applicable financial reporting framework.</p> <p>Note: AS 2815, <i>The Meaning of "Present Fairly in Conformity With Generally Accepted Accounting Principles,"</i> establishes requirements for evaluating the presentation of the financial statements. AS 2820, <i>Evaluating Consistency of Financial Statements,</i> establishes requirements regarding evaluating the consistency of the accounting principles used in financial statements.</p> <p>Note: The auditor should look to the requirements of the Securities and Exchange Commission for the company under audit with respect to the accounting principles applicable to that company.</p>	Issuer F