

**Report on**  
**2017 Inspection of Deloitte & Touche LLP**  
**(Headquartered in New York, New York)**

**Issued by the**  
**Public Company Accounting Oversight Board**

**December 20, 2018**

**THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT**  
**PORTIONS OF THE COMPLETE REPORT ARE OMITTED**  
**FROM THIS DOCUMENT IN ORDER TO COMPLY WITH**  
**SECTIONS 104(g)(2) AND 105(b)(5)(A)**  
**OF THE SARBANES-OXLEY ACT OF 2002**

**2017 INSPECTION OF DELOITTE & TOUCHE LLP**

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## EXECUTIVE SUMMARY

In 2017, the Public Company Accounting Oversight Board ("PCAOB" or "the Board") conducted an inspection of the registered public accounting firm Deloitte & Touche LLP ("the Firm") pursuant to the Sarbanes-Oxley Act of 2002 ("the Act"). The inspection procedures included reviews of portions of the Firm's work on 55 issuer audits, which generally related to issuer year ends in 2016.

The inspection team identified matters that it considered to be deficiencies in the performance of the work it reviewed. In 11 audits, certain of these deficiencies 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. These deficiencies are described in Part I.A of the report.

The Board cautions against using the number of audits with deficiencies in the public portion of a report to draw conclusions about the frequency of deficiencies throughout the firm's practice. The audits to be reviewed are most often selected based on perceived risk and not through a practice designed to identify a representative sample that could be extrapolated to the firm's entire practice. The portions of these audits that are reviewed often involve the most risky areas of the financial statements. Thus, much of the audit work that is inspected presents, in the inspection team's view, a heightened possibility of auditing deficiencies.

In the 2017 inspection, the inspection team also assessed the Firm's system of quality control related to issuer audits. Pursuant to the Act, any criticisms or discussions of defects or potential defects in that system will remain nonpublic unless the Firm fails to address those criticisms or defects to the Board's satisfaction, within 12 months of the issuance of this report.

### *Audit Opinions Affected by the Identified Deficiencies*

Fifty-two of the 55 engagements inspected were integrated audits of both internal control and the financial statements. As depicted in the table below, the inspection team identified deficiencies in both financial statement audits and audits of internal control over financial reporting ("ICFR"). In one of the audits described in Part I.A of this report, after the primary inspection procedures, the Firm revised its opinion on the effectiveness of the issuer's ICFR to express an adverse opinion.

	Number of Audits
<b>Audits for which deficiencies included in Part I.A related to both the financial statement audit and the ICFR audit</b>	<u>2 Audits</u> : Issuers F and H
<b>Audits for which deficiencies included in Part I.A related to the ICFR audit only</b>	<u>6 Audits</u> : Issuers A, B, E, G, I, and J
<b>Audits for which deficiencies included in Part I.A related to the financial statement audit only</b>	<u>3 Audits</u> : Issuers C, D, and K
<b>Total</b>	11

*Most Frequently Identified Audit Deficiencies*

The following table lists, in summary form, the types of deficiencies that appear most frequently in Part I.A of this report and shows which issuer audits included these deficiencies.

Issue	Part I.A Audits
<b>Failure to sufficiently test the design and/or operating effectiveness of controls that included a review element and that the Firm selected for testing</b>	<u>7 Audits</u> : Issuers A, B, E, F, G, H, and I
<b>Failure to identify and test any controls that addressed the risks related to a particular account or assertion</b>	<u>3 Audits</u> : Issuers E, F, and H
<b>Failure to test that the relevant criteria for revenue recognition were met</b>	<u>3 Audits</u> : Issuers C, D, and F

*Areas in which Audit Deficiencies Were Most Frequently Identified*

The following table lists, in summary form, the three financial statement accounts or auditing areas in which the deficiencies that are included in Part I.A of this report most frequently occurred.

Area	Part I.A Audits
<b>Revenue, including deferred revenue</b>	<u>6 Audits</u> : Issuers C, D, E, F, H, and I
<b>Business combinations</b>	<u>2 Audits</u> : Issuers E and F
<b>Inventory</b>	<u>2 Audits</u> : Issuers E and K

## **PART I**

### **INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS**

Inspections are designed and performed to assess compliance with applicable standards and requirements. The inspection team reviews both (1) selected audits and (2) policies and procedures related to quality control processes. The primary procedures<sup>1</sup> for the inspection were performed from October 2016 to April 2018. Inspectors conducted field work at the Firm's National Office and inspected issuer audits performed by 31 of the Firm's approximately 62 U.S. practice offices.

Part I.A includes a description of all audit deficiencies that reach a defined level of significance, which is described below. These deficiencies are categorized in various ways in both Part I.B and the Executive Summary. Part I.C of this report provides certain demographic information about all of the audits inspected. Part I.D provides a general description of the procedures performed in an annual inspection.

Inspections are designed to identify deficiencies in audit work and defects or potential defects in the firm's system of quality control. This focus on deficiencies and defects necessarily carries through to inspection reports and, therefore, the reports are not intended as balanced report cards or overall rating tools. Further, the lack of discussion within a report of an aspect of the inspected firm's quality control system should not be interpreted to imply that the Board has reached a conclusion about that aspect. Similarly, 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, an 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 described in that report.

The inspection team's evaluation of the Firm's quality control system included both (1) a review of certain aspects of the Firm's quality control system and (2) an assessment of whether the deficiencies identified in individual audits indicate defects or potential defects in the Firm's quality control system.

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<sup>1</sup> 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.

## A. Review of Audit Engagements

The inspection procedures included reviews of portions of 54 issuer audits performed by the Firm and a review of the Firm's audit work on one other issuer audit engagement in which the Firm played a role but was not the principal auditor.

Certain of the deficiencies were of such significance that the inspection team determined that the Firm issued an opinion without obtaining sufficient appropriate audit evidence that the financial statements were free of material misstatement and/or the issuer maintained effective ICFR. These deficiencies are described in Part I.A. The descriptions in Part I.A include references to the auditing standards that most directly relate to those deficiencies. (See Appendix B for the text of these standards.) References to provisions of the auditing standards that generally address all aspects of the audit are provided only when lack of compliance with these standards is the primary reason for the deficiency.<sup>2</sup>

Inclusion in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the firm's attention. In many cases, the Firm has since performed remedial actions intended to address the deficiencies.<sup>3</sup> That an audit deficiency reached the level of significance to be included in Part I.A of an inspection report does not mean that the financial statements are misstated or that there are undisclosed material weaknesses in ICFR. It is often not possible for the inspection team to reach a conclusion on those points because the inspection team usually has only the information the auditor retained and the issuer's public disclosures. Even when not associated with a disclosed misstatement or previously unidentified material weakness, an auditor's failure to obtain sufficient appropriate audit evidence is a serious matter.

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<sup>2</sup> These broadly applicable provisions are described in Part I.B of this report.

<sup>3</sup> 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 prevent reliance on its previously expressed audit opinions. An inspection normally includes a review, on a sample basis, 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 could be a basis for criticisms of the firm's quality control system or Board disciplinary sanctions.

The audit deficiencies that were so significant that it appeared that the audit opinion was unsupported are described in Parts I.A.1 through I.A.11, below. Issuer audits are generally presented in the order of significance of the deficiencies identified in the inspections of those audits; severity is assessed based on extent of the deficiencies identified in the audit, financial statement accounts affected, and/or potential consequences of the audit deficiency.

### *Audit Deficiencies*

#### A.1. Issuer A

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

- The Firm's procedures to test controls over the valuation of a significant portion of the issuer's investment portfolio were insufficient. This portion consisted of investments either that were categorized as level 3 within the hierarchy set forth in Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 820, *Fair Value Measurement*, or the value of which had a significant effect on certain income statement accounts. The Firm selected for testing three controls over the assumptions used in the valuation of these investments –
  - The first control consisted of a review of the issuer's valuation guidelines, which set forth a range of possible assumptions to be used to value these investments. The Firm's procedures to test this control were limited to inquiring of the control owner, inspecting the support for a change to the guidelines for one of the assumptions, and inspecting emails evidencing the control owner's approval of the valuation guidelines.
  - The second control consisted of a review of the reasonableness of the specific assumptions used in the valuation of these investments, including an evaluation of whether the assumptions were consistent with the issuer's valuation guidelines. The Firm's procedures to test this control were limited to inquiring of certain control owners, inspecting the support reviewed by the control owners to evaluate whether the assumptions were consistent with the valuation guidelines, and obtaining evidence of the control owners' approval.

- The third control consisted of meetings to review and approve the conclusions resulting from the second control. The Firm's procedures to test this control were limited to inquiring of the meeting attendees, inspecting the documents discussed in the meetings, and inspecting the meeting minutes.

For each of these three controls, the Firm failed to evaluate the nature of the review procedures performed, including the criteria used by the control owners to identify matters for follow up and whether those matters were appropriately resolved. (AS 2201.42 and .44)

- The Firm's procedures to test controls over the valuation of, and disclosures related to, another significant portion of the issuer's investment portfolio, which was categorized as level 2 within the hierarchy set forth in FASB ASC Topic 820, were insufficient. The Firm selected for testing two controls that consisted of reviews of the valuation of those investments that had missing, stale, or potentially unrealizable values. The control owners used four reports to identify the investments that met these criteria. While the Firm tested information technology general controls over the system that generated these reports, it failed to identify and test any controls over the completeness of the information within three of the four reports. (AS 2201.39)

#### A.2. Issuer B

In this audit of an insurance provider operating in the health care industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the effectiveness of ICFR. Specifically –

- For one of its segments, the issuer estimated the incurred but not reported claims, which represented a significant portion of total liabilities, using loss triangles that included monthly historical claims incurred and claims paid for multiple periods ("historical data"). The Firm identified a risk of material misstatement related to the possible use of inaccurate data to estimate this liability. The Firm selected for testing three controls that consisted of comparisons of the historical data totals to the claims processing systems and the general ledger. These controls, however, were not designed to address the risk of material misstatement related to whether the historical data were included in the loss triangles in the appropriate period and in the appropriate amount, and the Firm failed to identify and test any other controls that did so. (AS 2201.39)



- For another of the issuer's segments, the Firm selected for testing a control that included a review of the assumptions used to estimate the liability for future policy benefits, which represented a significant portion of the issuer's total liabilities. The Firm's procedures to test this aspect of the control were limited to inquiring of the control owners and reading correspondence between management and the issuer's external actuary regarding changes to an assumption for one product. The Firm failed to ascertain and evaluate the nature of the specific procedures that the control owners performed. (AS 2201.42 and .44)

### A.3. Issuer C

In this audit of an issuer in the information technology industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements. The majority of the issuer's revenue was derived from multiple-element arrangements. These arrangements included (1) a software deliverable billed as base license fees and license fees related to transaction volume (collectively, "total license fees") and (2) a maintenance deliverable, which consisted of software updates and product support services, with stated renewal rates. The issuer used the stated renewal rates for the maintenance deliverable as vendor-specific objective evidence ("VSOE") of fair value when the stated renewal rates were considered to be substantive. The issuer determined whether the renewal rates for the maintenance deliverable were substantive based on analyses of whether the maintenance renewal rate as a percentage of the base license fees did not fall significantly below a range indicative of normal pricing practices. Based on these analyses, the issuer concluded that VSOE did exist, and it recognized the consideration allocated to the software deliverable as revenue upon delivery of the software to the customer and the consideration allocated to the maintenance deliverable ratably over the term of the arrangement. The Firm failed to perform sufficient procedures to evaluate whether the stated renewal rates for maintenance were substantive, as follows –

- There was significant variation in the ratio of the license fees related to transaction volume to the total license fees for the issuer's contracts. The issuer, however, considered only the base license fees when determining whether the stated renewal rates for maintenance were substantive. The Firm failed to evaluate whether this exclusion of the license fees related to transaction volume from the determination was appropriate. (AS 2810.30)
- In evaluating whether the stated renewal rates for maintenance were representative of the price the customer would be required to pay when

the maintenance is sold separately, the Firm failed to take into account its understanding that the software updates included in the maintenance deliverables were generally critical to the customers' operations. (AS 2810.30)

A.4. Issuer D

In this audit of an issuer in the health care industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements, as its procedures to test revenue were insufficient. The issuer recognized revenue upon the sale of its products to distributors based, in part, on having the ability to reliably estimate product returns and rebate reserves ("revenue deductions"). The Firm performed procedures to test the issuer's estimates of revenue deductions and concluded that there was sufficient, reliable data available to develop these estimates. The Firm, however, also identified deficiencies in the issuer's controls over these estimates, as well as significant audit adjustments to these estimates that resulted, in part, from the issuer's use of unsupported assumptions in its calculation of revenue deductions. The Firm failed to evaluate whether the identified control deficiencies and audit adjustments were an indication that the issuer lacked the ability to reliably estimate revenue deductions, despite the availability of sufficient, reliable data, and, if so, whether it was appropriate for the issuer to recognize revenue upon the sale of its products to distributors. (AS 2810.30)

A.5. Issuer E

In this audit of an issuer in the health care industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the effectiveness of ICFR –

- For certain of the issuer's subsidiaries, which generated a significant portion of total revenue, the issuer entered into contracts that contained multiple deliverables. For each contract, the contract terms, the identified deliverables, and the amount of consideration allocated to each deliverable were entered into the issuer's system to create sales orders and record revenue. The Firm failed to identify and test any controls over the accuracy and completeness of the entry of these data into the issuer's system. (AS 2201.39)
- During the year, the issuer acquired a business, and it used cash-flow forecasts to determine the fair value of certain acquired intangible assets. The Firm selected for testing a control over the accounting for business

combinations that included a review of the reasonableness of the assumptions used in the cash-flow forecasts. The Firm's procedures to test this aspect of the control consisted of inquiring of management and inspecting emails for evidence of review and approval. The Firm failed to evaluate the nature of the review procedures performed by the control owner, including the criteria used to identify matters for follow up and the resolution of those matters. (AS 2201.42 and .44)

- The Firm's procedures related to controls over the existence of the majority of the issuer's inventory were insufficient. The Firm identified and tested one control that consisted of a review of the issuer's reconciliation of its cycle-count results to the inventory system and its investigation of variances for individual items. This control was not designed to address the sufficiency of the inventory items counted, the frequency of the counts, and the aggregate deviations identified in the counts, and the Firm failed to identify and test any other controls that did so. (AS 2201.39)

#### A.6. Issuer F

In this audit of an issuer in the industrials industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and on the effectiveness of ICFR. Specifically –

- The Firm's procedures to test revenue for many of the issuer's locations, which represented a significant portion of the issuer's total revenue and which the Firm determined presented a risk of material misstatement in the aggregate, consisted of (1) testing entity-level controls consisting of reviews of financial results, (2) performing tests of transaction-level controls and tests of details related to revenue at three of these locations, and (3) performing analytical procedures. The Firm's substantive procedures were insufficient, as the tests of details provided assurance only for the three locations subjected to that testing; the untested locations, in the aggregate, were multiple times the Firm's established level of materiality and presented a reasonable possibility of material misstatement. The analytical procedures that were performed for certain of these locations provided little to no substantive assurance as they were performed as part of the Firm's risk assessment and were not designed to provide substantive assurance. (AS 2301.08)

- The Firm's procedures related to revenue recognized from multiple-element arrangements for one of the issuer's segments, which was multiple times the Firm's established level of materiality, were insufficient as described below.
  - The Firm identified and tested three controls to address the risk of material misstatement related to this revenue, including the risk related to the identification of units of accounting. These controls consisted of (1) the annual review of whether products sold to customers during the year had a stand-alone value, (2) the review of adjustments to record the delivered elements based on their relative selling prices, and (3) the review of the recording and reconciliation of deferred revenue. These controls, however, were not designed to address the evaluation of whether the deliverables in these arrangements represented separate units of accounting, and the Firm failed to identify and test any other controls that did so. (AS 2201.39)
  - The Firm failed to perform any substantive procedures to test whether the deliverables identified within these multiple-element arrangements represented separate units of accounting. (AS 2810.30)
- During the year, the issuer acquired a business, and it used cash-flow forecasts to determine the fair value of certain acquired intangible assets. The Firm selected for testing two controls over the accounting for business combinations that included a review of the revenue and profit margin assumptions used in the cash-flow forecasts. The Firm's procedures to test these controls consisted of (1) inquiring of the control owners, (2) inspecting evidence that indicated the reviews had occurred, (3) testing the mathematical accuracy of certain calculations, and (4) comparing certain amounts used in the valuation to other documentation. The Firm, however, failed to evaluate the nature of the procedures performed by the control owners to review the revenue and profit margin assumptions that the issuer used in the forecasts, including the criteria used to identify matters for follow up and the resolution of those matters. (AS 2201.42 and .44)

A.7. Issuer G

In this audit of an issuer in the health care industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the effectiveness of ICFR, as its procedures to test controls over goodwill were insufficient. The issuer performed analyses to assess the possible impairment of goodwill, and to determine the amount of recorded impairment charges, using the income approach and the market approach. The Firm selected for testing four controls over goodwill that included reviews of the following significant assumptions used in these analyses: (1) revenue and profit margin multiples used in the market approach, (2) forecasted revenue growth rates and profit margins used in the income approach, and (3) the fair value of long-lived assets used in the measurement of the impairment charge. The Firm limited its procedures to test the aspects of these controls related to these assumptions to (1) inquiring of the control owners and comparing certain information provided by one control owner to the prior-year work papers for consistency; (2) obtaining and inspecting certain documents created or used in the operation of the controls; (3) for one control, inspecting an email as evidence that the review had occurred; and (4) for another control, tracing certain amounts to the general ledger. The Firm failed to evaluate the nature of the review procedures performed by the control owners regarding these assumptions, including the criteria used to identify matters for follow up and the resolution of such matters. (AS 2201.42 and .44)

A.8. Issuer H

In this audit of an issuer in the information technology industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and on the effectiveness of ICFR. The issuer used a service organization to process transactions for a significant portion of its total revenue. The Firm's procedures related to this revenue were insufficient. Specifically –

- The Firm obtained a service auditor's report that described certain complementary user controls that the issuer needed to have in place in order to achieve the control objectives described in the service auditor's report. Those complementary controls included (1) a control over the accuracy and completeness of the customer data provided to the service organization and (2) a control to review the accuracy of the amounts billed by the service organization. The Firm identified and tested one control that it intended to address the objectives of these complementary controls. This control consisted of (1) a review of monthly customer billing amounts, and an investigation of differences from prior-month amounts above an established threshold, and (2) a review of monthly revenue journal entries

and related revenue amounts. This control, however, did not address the accuracy and completeness of customer data provided to the service organization, and the Firm failed to identify and test any other control that did so. In addition, the Firm's procedures to test the aspect of the control that addressed the accuracy of the amounts billed by the service organization were insufficient, as its procedures were limited to inquiring of the control owner. (AS 2201.39, .42, .44, and .B22)

- The Firm designed certain of its substantive procedures – including its sample sizes – based on a level of control reliance that was not supported due to the deficiencies in the Firm's testing of controls that are described above. As a result, the sample sizes the Firm used to test this revenue were too small to provide sufficient evidence. (AS 2301.16, .18, and .37; AS 2315.19, .23, and .23A)

#### A.9. Issuer I

In this audit of an issuer in the energy industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the effectiveness of ICFR, as its procedures to test controls over revenue were insufficient. The issuer recognized a majority of its revenue using the percentage-of-completion method of accounting. The Firm selected for testing three controls that addressed the occurrence and allocation of revenue; these controls involved monthly reviews of reports related to the status of each project, including estimated costs to complete and gross margin by project. The Firm's procedures to test the operating effectiveness of two of the controls consisted of inquiring of the control owners and inspecting documentation evidencing the control owners' reviews. The Firm, however, failed to (1) determine whether the control owners used the established criteria for investigation and (2) ascertain, in most of the instances selected for testing, whether the items identified for follow up were resolved. The Firm concluded that the third control would operate at a level of precision that could detect a material misstatement only in combination with one of the other two controls, and its procedures to test that control were not sufficient as described above. (AS 2201.44)

#### A.10. Issuer J

In this audit of an issuer in the industrials industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the effectiveness of ICFR. The Firm determined that five of the controls that it identified and selected for testing were not effective. The Firm and the issuer evaluated the severity of the deficiencies associated with these five controls and concluded that the deficiencies

represented material weaknesses related to relevant assertions for certain significant accounts. Certain of the controls with deficiencies were also identified to address relevant assertions for other significant accounts. The Firm, however, failed to evaluate whether these deficiencies represented additional material weaknesses. (AS 2201.62)

#### A.11. Issuer K

In this audit of an issuer in the industrials industry sector, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements, as its procedures to test the existence of inventory were not sufficient. The issuer's in-transit inventory and inventory held at public warehouses in foreign locations each totaled more than double the Firm's established level of materiality. For in-transit inventory, the Firm failed to perform any procedures. For the inventory held at the foreign external warehouses, which represented a significant proportion of the issuer's current assets, the Firm's only procedure was to obtain confirmations from the custodians, which was insufficient given the significance of the inventory held at these warehouses. (AS 2301.36; AS 2510.14)

### **B. Auditing Standards**

Each deficiency described in Part I.A above could relate to several provisions of the auditing standards that govern the conduct of audits. The paragraphs of the standards that are cited in Part I.A for each deficiency are only 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. Appropriateness is the measure of the quality of audit evidence; to be appropriate, evidence must be both relevant and reliable in providing support for the related conclusions.

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 References per Audit
<b><i>AS 2201, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements</i></b>	Issuer A	2
	Issuer B	2
	Issuer E	3
	Issuer F	2
	Issuer G	1
	Issuer H	1
	Issuer I	1
	Issuer J	1
<b><i>AS 2301, The Auditor's Responses to the Risks of Material Misstatement</i></b>	Issuer F	1
	Issuer H	1
	Issuer K	1
<b><i>AS 2315, Audit Sampling</i></b>	Issuer H	1
<b><i>AS 2510, Auditing Inventories</i></b>	Issuer K	1
<b><i>AS 2810, Evaluating Audit Results</i></b>	Issuer C	2
	Issuer D	1
	Issuer F	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 2201	AS 2301	AS 2315	AS 2510	AS 2810
<b>Business combinations</b>	E, F				
<b>Impairment of goodwill</b>	G				
<b>Income taxes</b>	J				
<b>Insurance-related assets and insurance-related liabilities, including insurance reserves</b>	B				
<b>Inventory</b>	E	K		K	
<b>Investment securities</b>	A				
<b>Revenue, including deferred revenue</b>	E, F, H, I	F, H	H		C, D, F

**B.3. Audit Deficiencies by Industry**

The table below lists the industries<sup>4</sup> 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.

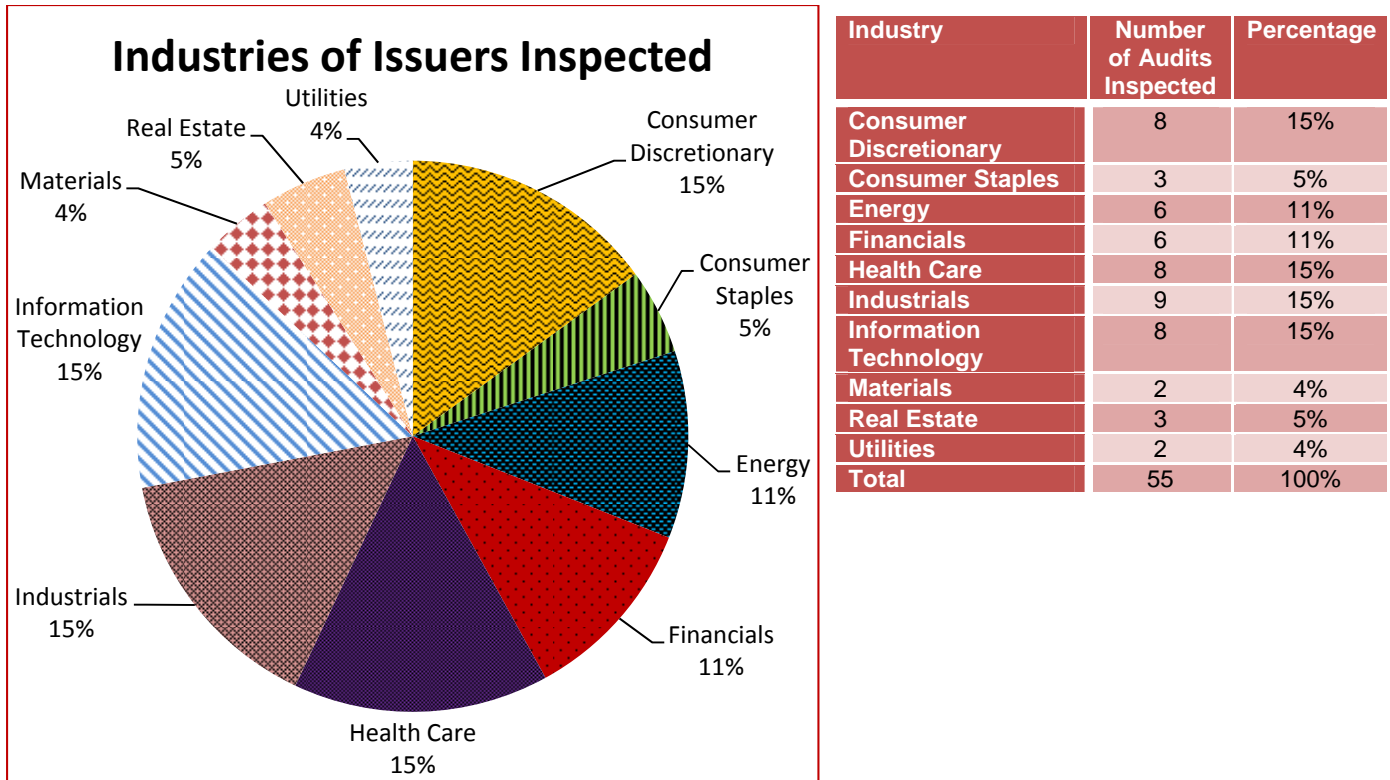
	AS 2201	AS 2301	AS 2315	AS 2510	AS 2810
<b>Energy</b>	I				
<b>Financials</b>	A				
<b>Health Care</b>	B, E, G				D
<b>Industrials</b>	F, J	F, K		K	F
<b>Information Technology</b>	H	H	H		C

<sup>4</sup> 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.

**C. Data Related to the Issuer Audits Selected for Inspection<sup>5</sup>**

**C.1. Industries of Issuers Inspected**

The chart below categorizes the 55 issuers whose audits were inspected in 2017, based on the issuer's industry.<sup>6</sup>

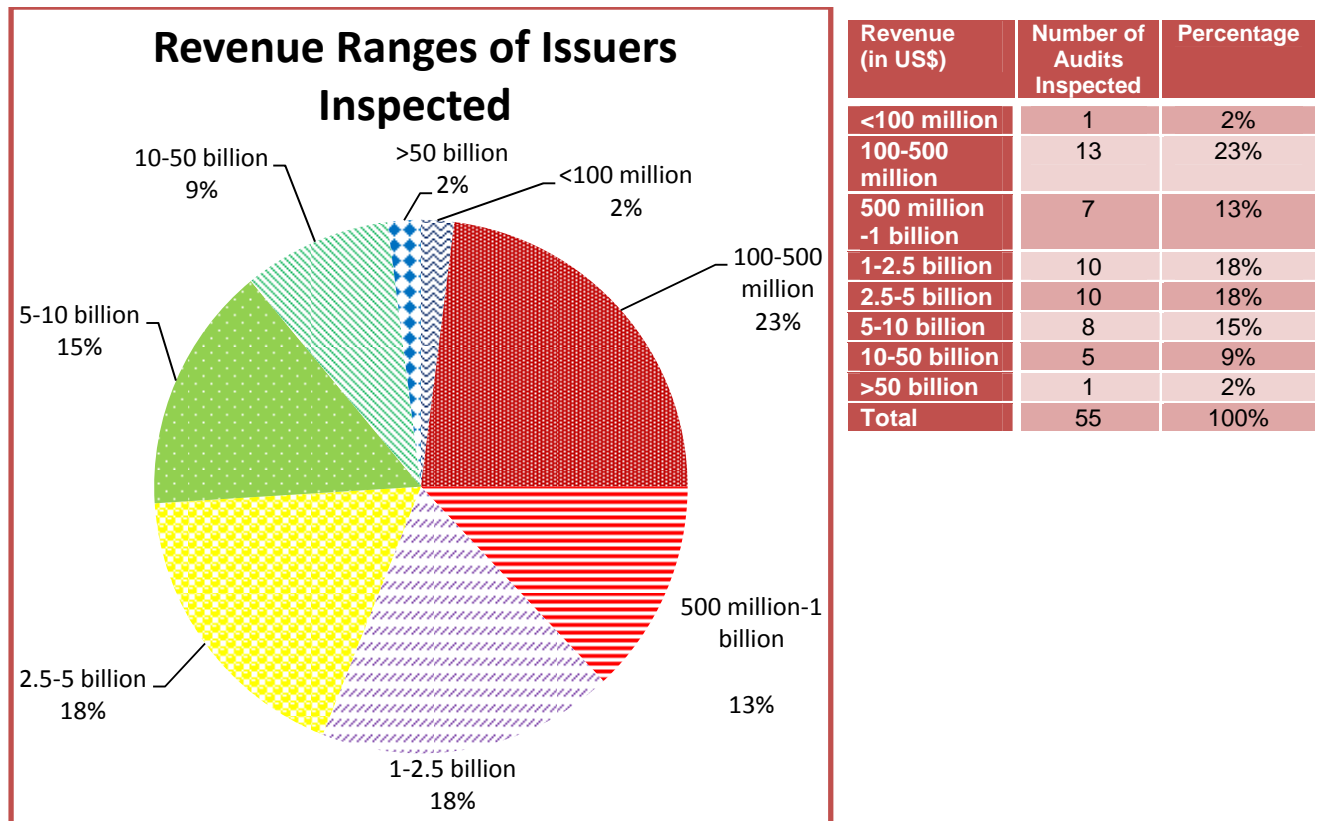


<sup>5</sup> Where the audit work inspected related to an engagement in which the Firm played a role but was not the principal auditor, the industry and the revenue included in the tables and charts in this section are those of the entity for which an audit report was issued by the primary auditor. As discussed above, the inspection process included reviews of portions of 54 selected issuer audits completed by the Firm and the Firm's audit work on one other issuer audit engagement in which it played a role but was not the principal auditor.

<sup>6</sup> 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 55 issuers whose audits were inspected in 2017.<sup>7</sup> This presentation of revenue data is intended to provide information related to the size of issuers whose audits 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.



<sup>7</sup> 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**

This section provides a brief description of the procedures that are often performed in annual inspections of auditing firms.

**D.1. Reviews of Audit Work**

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 review of any 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.<sup>8</sup>

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,<sup>9</sup> as well as a firm's failure to perform, or

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<sup>8</sup> 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 adjudicative process and do not constitute conclusive findings for purposes of imposing legal liability.

<sup>9</sup> 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

to perform sufficiently, certain necessary risk assessment procedures, tests of controls, and substantive audit procedures.

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, 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.

#### 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

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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.

potential defect in a firm's quality control system.<sup>10</sup> 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 the deficiencies;<sup>11</sup> 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 (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.

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<sup>10</sup> 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.

<sup>11</sup> 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.

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 firm personnel, including firm 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 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 processes 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 and operation of the firm's internal inspection program, and may compare the results of its review 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

PARTS II AND III OF THIS REPORT ARE NONPUBLIC  
AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

## **APPENDIX A**

### **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.<sup>12</sup>

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<sup>12</sup> 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 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.

December 14, 2018

Mr. George Botic  
Director  
Division of Registration and Inspections  
Public Company Accounting Oversight Board  
1666 K Street NW  
Washington, DC 20006

Re: Deloitte & Touche LLP – Response to Part I of Draft Report on 2017 Inspection (PUBLIC)

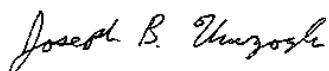
Dear Mr. Botic:

Deloitte & Touche LLP is pleased to submit this response to the draft Report on the 2017 Inspection of Deloitte & Touche LLP (the Draft Report) of the Public Company Accounting Oversight Board (the PCAOB or the Board). We believe that the PCAOB's inspection process serves an important role in the achievement of our shared objectives of improving audit quality and serving investors and the public interest. We are committed to continuing to work with the PCAOB to further strengthen trust in the integrity of the independent audit.

We have evaluated the matters identified by the Board's inspection team for each of the issuer audits described in Part I of the Draft Report and have taken actions as appropriate in accordance with PCAOB standards to comply with our professional responsibilities under AS 2901, *Consideration of Omitted Procedures After the Report Date*, and AS 2905, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*.

Executing high quality audits is our number one priority. In order to drive continuous improvements in quality, we are transforming the audit to leverage innovative technologies, along with enhancing the skillsets of our talent to prepare them for a digitally driven future. We are confident that our ongoing digital transformation, along with the investments we continue to make in our audit processes, policies, and quality controls, are resulting in significant enhancements to our audit quality.

Sincerely,



Joseph B. Ucuzoglu  
Chairman and Chief Executive Officer  
Deloitte & Touche LLP



Catherine M. Engelbert  
Chief Executive Officer  
Deloitte

In the United States, Deloitte refers to one or more of the US member firms of Deloitte Touche Tohmatsu Limited, their related entities that operate using the "Deloitte" name in the United States and their respective affiliates. Please see [www.deloitte.com/us/about](http://www.deloitte.com/us/about) for a detailed description of our legal structure.

**APPENDIX B**

**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>.

<b>AS 2201, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements</b>		
<b>USING A TOP-DOWN APPROACH</b>		
<b>Selecting Controls to Test</b>		
AS 2201.39	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.	Issuers A, B, E, F, and H
<b>TESTING CONTROLS</b>		
<b>Testing Design Effectiveness</b>		
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 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>	Issuers A, B, E, F, G, and H

<b>AS 2201, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements</b>		
<b>Testing Operating Effectiveness</b>		
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, E, F, G, H, and I
<b>EVALUATING IDENTIFIED DEFICIENCIES</b>		
AS 2201.62	<p>The auditor must evaluate the severity of each control deficiency that comes to his or her attention to determine whether the deficiencies, individually or in combination, are material weaknesses as of the date of management's assessment. In planning and performing the audit, however, the auditor is not required to search for deficiencies that, individually or in combination, are less severe than a material weakness.</p>	Issuer J
<b>APPENDIX B - Special Topics</b>		
<b>USE OF SERVICE ORGANIZATIONS</b>		
AS 2201.B22	<p>If the service auditor's report on controls placed in operation and tests of operating effectiveness contains a qualification that the stated control objectives might be achieved only if the company applies controls contemplated in the design of the system by the service organization, the auditor should evaluate whether the company is applying the necessary procedures.</p>	Issuer H

<b>AS 2301, <i>The Auditor's Responses to the Risks of Material Misstatement</i></b>		
<b>RESPONSES INVOLVING THE NATURE, TIMING, AND EXTENT OF AUDIT PROCEDURES</b>		
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.	Issuer F
<b>TESTING CONTROLS</b>		
<b>Testing Controls in an Audit of Financial Statements</b>		
AS 2301.16	<i>Controls to be Tested.</i> If the auditor plans to assess control risk at less than the maximum by relying on controls, <sup>12</sup> and the nature, timing, and extent of planned substantive procedures are based on that lower assessment, the auditor must obtain evidence that the controls selected for testing are designed effectively and operated effectively during the entire <b>period of reliance</b> . <sup>13</sup> However, the auditor is not required to assess control risk at less than the maximum for <i>all</i> relevant assertions and, for a variety of reasons, the auditor may choose not to do so.	Issuer H
<p><u>Footnotes to AS 2301.16</u></p> <p><sup>12</sup> Reliance on controls that is supported by sufficient and appropriate audit evidence allows the auditor to assess control risk at less than the maximum, which results in a lower assessed risk of material misstatement. In turn, this allows the auditor to modify the nature, timing, and extent of planned substantive procedures.</p> <p><sup>13</sup> Terms defined in Appendix A, <i>Definitions</i>, are set in <b>boldface type</b> the first time they appear.</p>		
AS 2301.18	<i>Evidence about the Effectiveness of Controls in the Audit of Financial Statements.</i> In designing and performing tests of controls for the audit of financial statements, the evidence necessary to support the auditor's control risk assessment depends on the degree of reliance the auditor plans to place on the effectiveness of a control. The auditor should obtain more persuasive audit evidence from tests of controls the greater the reliance the auditor places on the effectiveness of a control. The auditor also should obtain more persuasive evidence about the effectiveness of controls for each relevant assertion for which the audit approach consists primarily of tests of controls, including situations in which substantive procedures alone cannot provide sufficient appropriate audit evidence.	Issuer H

<b>AS 2301, <i>The Auditor's Responses to the Risks of Material Misstatement</i></b>		
<b>SUBSTANTIVE PROCEDURES</b>		
AS 2301.36	The auditor should perform substantive procedures for each relevant assertion of each significant account and disclosure, regardless of the assessed level of control risk.	Issuer K
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 H

<b>AS 2315, <i>Audit Sampling</i></b>		
<b>SAMPLING IN SUBSTANTIVE TESTS OF DETAILS</b>		
<b>Planning Samples</b>		
AS 2315.19	After assessing and considering the levels of inherent and control risks, the auditor performs substantive tests to restrict detection risk to an acceptable level. As the assessed levels of inherent risk, control risk, and detection risk for other substantive procedures directed toward the same specific audit objective decreases, the auditor's allowable risk of incorrect acceptance for the substantive tests of details increases and, thus, the smaller the required sample size for the substantive tests of details. For example, if inherent and control risks are assessed at the maximum, and no other substantive tests directed toward the same specific audit objectives are performed, the auditor should allow for a low risk of incorrect acceptance for the substantive tests of details. <sup>3</sup> Thus, the auditor would select a larger sample size for the tests of details than if he allowed a higher risk of incorrect acceptance.	Issuer H

Footnote to AS 2315.19

<sup>3</sup> Some auditors prefer to think of risk levels in quantitative terms. For example, in the circumstances described, an auditor might think in terms of a 5 percent risk of incorrect acceptance for the substantive test of details. Risk levels used in sampling applications in other fields are not necessarily relevant in determining appropriate levels for applications in auditing because an audit includes many interrelated tests and sources of evidence.



<b>AS 2315, Audit Sampling</b>		
AS 2315.23	<p>To determine the number of items to be selected in a sample for a particular substantive test of details, the auditor should take into account tolerable misstatement for the population; the allowable risk of incorrect acceptance (based on the assessments of inherent risk, control risk, and the detection risk related to the substantive analytical procedures or other relevant substantive tests); and the characteristics of the population, including the expected size and frequency of misstatements.</p>	Issuer H
AS 2315.23A	<p>Table 1 of the Appendix describes the effects of the factors discussed in the preceding paragraph on sample sizes in a statistical or nonstatistical sampling approach. When circumstances are similar, the effect on sample size of those factors should be similar regardless of whether a statistical or nonstatistical approach is used. Thus, when a nonstatistical sampling approach is applied properly, the resulting sample size ordinarily will be comparable to, or larger than, the sample size resulting from an efficient and effectively designed statistical sample.</p>	Issuer H

<b>AS 2510, Auditing Inventories</b>		
<b>INVENTORIES HELD IN PUBLIC WAREHOUSES</b>		
AS 2510.14	<p>If inventories are in the hands of public warehouses or other outside custodians, the auditor ordinarily would obtain direct confirmation in writing from the custodian. If such inventories represent a significant proportion of current or total assets, to obtain reasonable assurance with respect to their existence, the auditor should apply one or more of the following procedures as he considers necessary in the circumstances.</p> <ol style="list-style-type: none"> <li>a. Test the owner's procedures for investigating the warehouseman and evaluating the warehouseman's performance.</li> <li>b. Obtain an independent accountant's report on the warehouseman's control procedures relevant to custody of goods and, if applicable, pledging of receipts, or apply alternative procedures at the warehouse to gain reasonable assurance that information received from the warehouseman is reliable.</li> <li>c. Observe physical counts of the goods, if practicable and reasonable.</li> <li>d. If warehouse receipts have been pledged as collateral, confirm with lenders pertinent details of the pledged receipts (on a test basis, if appropriate).</li> </ol>	Issuer K

<b>AS 2810, Evaluating Audit Results</b>		
<b>EVALUATING THE PRESENTATION OF THE FINANCIAL STATEMENTS, INCLUDING THE DISCLOSURES</b>		
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, The Meaning of "Present Fairly in Conformity with Generally Accepted Accounting Principles," establishes requirements for evaluating the presentation of the financial statements. AS 2820, Evaluating Consistency of Financial Statements, 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>	Issuers C, D, and F