2018 Inspection Deloitte & Touche LLP

(Headquartered in New York, New York)

April 28, 2020

PCAOB

Public Company Accounting Oversight Board

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

PCAOB RELEASE NO. 104-2020-008

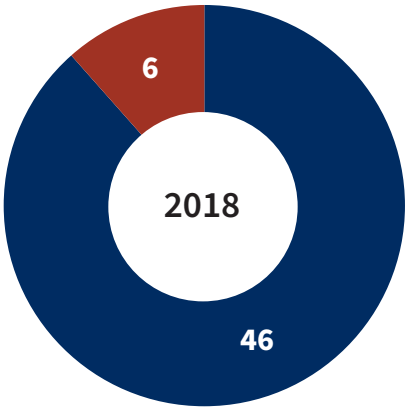
Executive Summary

Our 2018 inspection report on Deloitte & Touche LLP provides information on our inspection to assess the firm's compliance with Public Company Accounting Oversight Board ("PCAOB") standards and rules and other applicable regulatory and professional requirements. This executive summary offers a high-level overview of: (1) Part I.A of the report, which discusses deficiencies ("Part I.A deficiencies") in certain issuer audits that were of such significance that we believe the firm, at the time it issued its audit report(s), had not obtained sufficient appropriate audit evidence to support its opinion on the issuer's financial statements and/or internal control over financial reporting ("ICFR"), and (2) Part I.B of the report, which discusses deficiencies that do not relate directly to the sufficiency or appropriateness of evidence the firm obtained to support its opinion(s) but nevertheless relate to instances of non-compliance with PCAOB standards or rules.

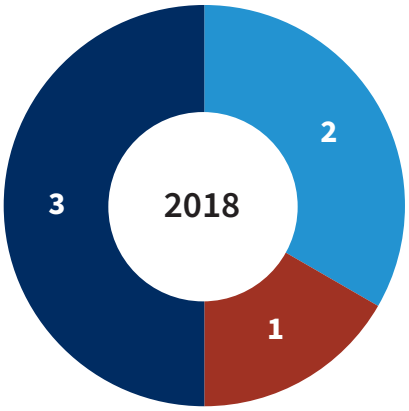
The fact that we have included a deficiency in this report — other than those deficiencies for audits with incorrect opinions on the financial statements and/or ICFR — does not necessarily mean that the issuer's financial statements are materially misstated or that undisclosed material weaknesses in ICFR exist. If a deficiency is included in Part I.A or Part I.B of this report, it does not necessarily mean that the firm has not addressed the deficiency.

Overview of the 2018 Deficiencies Included in Part I

Six of the 52 issuer audits we reviewed in 2018 are included in Part I.A of this report due to the significance of the deficiencies identified. The identified deficiencies related to the firm's testing of controls over and/or substantive testing of insurance-related assets and liabilities, including insurance reserves; investment securities; revenue and related accounts; and deposit liabilities.



Audits without Part I.A deficiencies
Audits with Part I.A deficiencies



Deficiencies in both financial statement and ICFR audits
Deficiencies in the financial statement audit only
Deficiencies in the ICFR audit only

The most common Part I.A deficiencies in 2018 related to testing controls over the accuracy and completeness of data or reports, testing the design or operating effectiveness of controls selected for testing, and evaluating significant assumptions or data that the issuer used in developing an estimate.

Other deficiencies identified during the 2018 inspection that do not relate directly to the sufficiency or appropriateness of evidence the firm obtained to support its opinion(s), which appear in Part I.B, related to retention of audit documentation and Form AP.

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2018 Inspection

During the PCAOB's 2018 inspection of Deloitte & Touche LLP, we assessed the firm's compliance with laws, rules, and professional standards applicable to the audits of public companies.

We selected for review 52 audits of issuers with fiscal years generally ending in 2017. For each issuer audit selected, we reviewed a portion of the audit. We also evaluated elements of the firm's system of quality control.

What's Included in this Inspection Report

This report includes the following sections:

- **Overview of the 2018 Inspection and Historical Data by Inspection Year:** Information on our inspection, historical data, and common deficiencies.
- **Part I – Inspection Observations:**
  - **Part I.A:** Deficiencies that were of such significance that we believe the firm, at the time it issued its audit report(s), had not obtained sufficient appropriate audit evidence to support its opinion on the issuer's financial statements and/or ICFR.
  - **Part I.B:** Deficiencies that do not relate directly to the sufficiency or appropriateness of evidence the firm obtained to support its opinion(s) but nevertheless relate to instances of non-compliance with PCAOB standards or rules.
- **Part II – Observations Related to Quality Control:** Criticisms of, or potential defects in, the firm's system of quality control. Section 104(g)(2) of the Sarbanes-Oxley Act ("the Act") restricts us from publicly disclosing Part II deficiencies unless the firm does not address the criticisms or potential defects to the Board's satisfaction no later than 12 months after the issuance of this report.
- **Appendix A – Firm's Response to the Draft Inspection Report:** The firm's response to a draft of this report, excluding any portion granted confidential treatment.

2018 Inspection Approach

In selecting issuer audits for review, we use both risk-based and random methods of selection. We make most selections based on (1) our internal evaluation of audits we believe have a heightened risk of material misstatement, including those with challenging audit areas, and (2) other risk-based characteristics, including issuer and firm considerations. We select the remaining audits randomly to provide an element of unpredictability.

When we review an audit, we do not review every aspect of the audit. Rather, we generally focus our attention on audit areas we believe to be of greater complexity, areas of greater significance or with a heightened risk of material misstatement to the issuer's financial statements, and areas of recurring deficiencies. We may also select some audit areas for review in a manner designed to incorporate unpredictability.

Our selection of audits for review does not constitute a representative sample of the firm's total population of issuer audits. Additionally, our inspection findings are specific to the particular portions of the issuer audits reviewed. They are not an assessment of all of the firm's audit work nor of all of the audit procedures performed for the audits reviewed.

View the details on the scope of our inspections and our inspections procedures.

Overview of the 2018 Inspection and Historical Data by Inspection Year

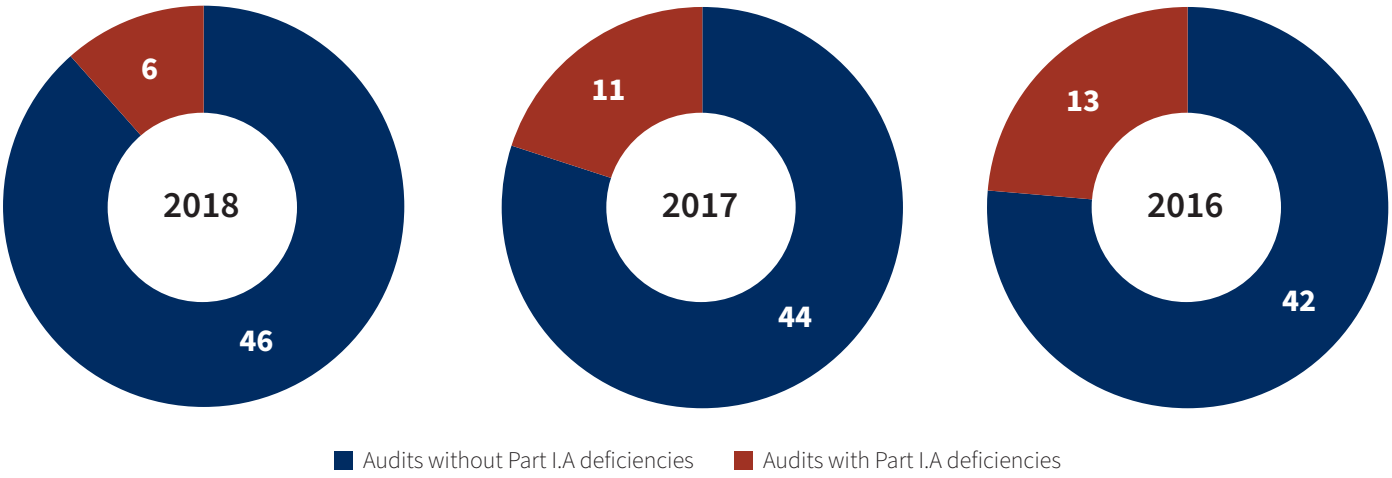
The following information provides an overview of our inspections in 2018 of the firm's issuer audits as well as data from the previous two inspections. We use a combination of risk-based and random methods to select audits for review and to identify areas on which we focus our inspection. Because our inspection process evolves over time, it can, and often does, focus on a different mix of audits and focus areas from year to year and firm to firm. As a result of this variation, we caution that our inspection results are not necessarily comparable over time or among firms.

Audits Reviewed

	2018	2017	2016
Total audits reviewed	52	55	55
Audits in which the firm was the principal auditor	51	54	54
Audits in which the firm was not the principal auditor	1	1	1
Integrated audits of financial statements and ICFR	49	52	53
Risk-based selections	42	45	45
Random selections	10	10	10

Part I.A Deficiencies in Audits Reviewed

In 2018 and 2017, all audits appearing in Part I.A were selected for review using risk-based criteria. In 2016, 12 of the 13 audits appearing in Part I.A were selected for review using risk-based criteria.

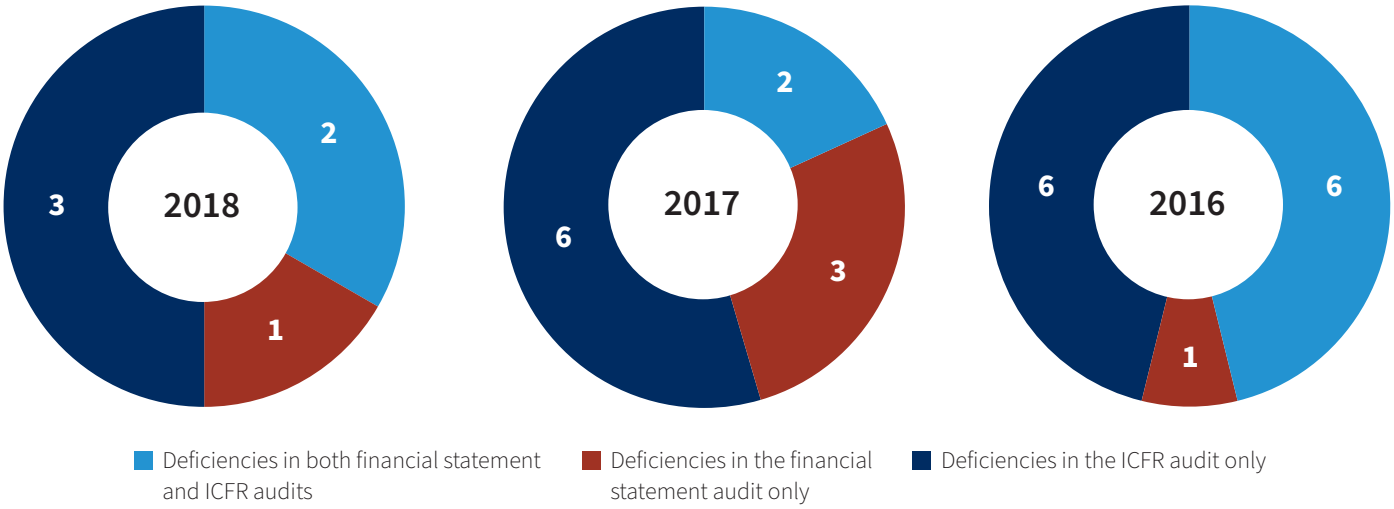


If a deficiency is included in Part I.A of our report, it does not necessarily mean that the firm has not addressed the deficiency. In many cases, the firm has performed remedial actions after the issue was identified. Depending on the circumstances, remedial actions may include performing additional audit procedures, informing management of the issuer of the need for changes to the financial statements or reporting on ICFR, or taking steps to prevent reliance on prior audit reports. Our inspection normally includes a review, on a sample basis, of the adequacy of a firm's remedial actions, either with respect to previously identified deficiencies or deficiencies identified during that inspection. If a

firm does not take appropriate actions to address deficiencies, we may criticize its system of quality control or pursue a disciplinary action.

The fact that we have included a deficiency in our report — other than those deficiencies for audits with incorrect opinions on the financial statements and/or ICFR — does not necessarily mean that the issuer's financial statements are materially misstated or that undisclosed material weaknesses in ICFR exist. It is often not possible for us to reach a conclusion on those points based on our inspection procedures and related findings because, for example, we have only the information that the auditor retained and the issuer's public disclosures. We do not have direct access to the issuer's management, underlying books and records, and other information.

Audits Affected by the Deficiencies Identified in Part I.A



In connection with our 2017 and 2016 inspection procedures for one audit in each year, the issuer revised its report on ICFR, and the firm revised its opinion on the effectiveness of the issuer's ICFR to express an adverse opinion and reissued its report.

The following tables and graphs summarize inspection-related information, by inspection year, for 2018 and the previous two inspections. We caution any comparison of the data provided without reading the descriptions of the underlying deficiencies in each respective inspection report.

Most Frequently Identified Part I.A Deficiencies

Deficiencies in audits of financial statements	Audits with Part I.A deficiencies		
	2018	2017	2016
Did not sufficiently evaluate significant assumptions or data that the issuer used in developing an estimate	2	0	5

Deficiencies in ICFR audits	Audits with Part I.A deficiencies		
	2018	2017	2016
Did not identify and/or sufficiently test controls over the accuracy and completeness of data or reports	3	2	4
Did not perform sufficient testing of the design and/or operating effectiveness of controls selected for testing	2	7	9

Audit Areas Most Frequently Reviewed

This table reflects the five focus areas we have selected most frequently for review in each inspection year (and the related Part I.A deficiencies). For the issuer audits selected for review, we selected these areas because they were generally significant to the issuer's financial statements, may have included complex issues for auditors, and/or involved complex judgments in (1) estimating and auditing the reported value of related accounts and disclosures and (2) implementing and auditing the related controls.

2018			2017			2016		
Audit area	Audits reviewed	Audits with Part I.A deficiencies	Audit area	Audits reviewed	Audits with Part I.A deficiencies	Audit area	Audits reviewed	Audits with Part I.A deficiencies
Revenue and related accounts	47	1	**Revenue and related accounts**	49	6	**Revenue and related accounts**	48	3
Business combinations	17	0	**Inventory**	22	2	**Inventory**	20	2
Inventory	16	0	**Goodwill and intangible assets**	21	1	**Goodwill and intangible assets**	16	1
Goodwill and intangible assets	12	0	**Long-lived assets**	15	0	**Long-lived assets**	15	3
Income taxes	10	0	**Business combinations**	11	2	**Business combinations**	10	1

Audit Areas with Frequent Part I.A Deficiencies

This table reflects the focus areas with the most frequently identified Part I.A deficiencies in each inspection year with the corresponding results for the other two years presented.

Audit area	2018		2017		2016	
	Audits with Part I.A deficiencies	Audits reviewed	Audits with Part I.A deficiencies	Audits reviewed	Audits with Part I.A deficiencies	Audits reviewed
Insurance-related assets and liabilities, including insurance reserves	3	5	1	3	0	2
Revenue and related accounts	1	47	6	49	3	48
Investment securities	1	7	1	7	3	8
Deposit liabilities	1	1	0	2	0	0
Inventory	0	16	2	22	2	20
Business combinations	0	17	2	11	1	10
Long-lived assets	0	9	0	15	3	15

Insurance-related assets and liabilities, including insurance reserves: The deficiencies in 2018 related to substantive testing of, and testing controls over, the accuracy of claims data used by the issuer to determine the estimated liabilities. The deficiencies in 2017 related to testing controls over insurance-related liabilities.

Revenue and related accounts: The deficiencies in 2018 related to testing controls over revenue. The deficiencies in 2017 and 2016 related to substantive testing of, and testing controls over, revenue.

Investment securities: The deficiencies in 2018, 2017, and 2016 primarily related to testing controls over the valuation of investment securities.

Deposit liabilities: The deficiency in 2018 related to substantive testing of the recorded balance of deposit liabilities.

Inventory: The deficiencies in 2017 related to substantive testing of the existence of inventory and testing cycle-count controls. The deficiencies in 2016 related to substantive testing of the existence and valuation of inventory and testing controls over the valuation of inventory.

Business combinations: The deficiencies in 2017 related to testing controls involving the issuer's review of assumptions used to value acquired intangible assets. The deficiencies in 2016 related to testing controls over the valuation of acquired loans.

Long-lived assets: The deficiencies in 2016 related to substantive testing of, and testing controls over, long-lived assets evaluated for potential impairment.

Auditing Standards Associated with Identified Part I.A Deficiencies

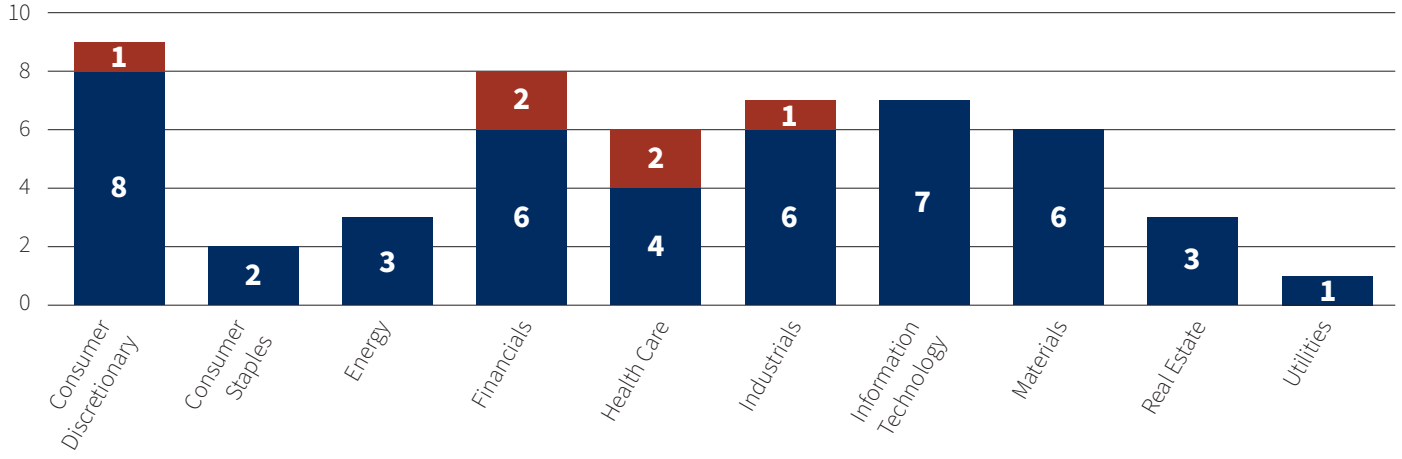
The following lists the auditing standards referenced in Part I.A of the 2018 and the previous two inspection reports and the number of times that the standard is cited in Part I.A.

PCAOB Auditing Standards	2018	2017	2016
AS 1105, *Audit Evidence*	2	0	1
AS 2110, *Identifying and Assessing Risks of Material Misstatement*	0	0	1
AS 2201, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*	5	13	21
AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*	0	3	4
AS 2305, *Substantive Analytical Procedures*	0	0	1
AS 2310, *The Confirmation Process*	1	0	0
AS 2315, *Audit Sampling*	0	1	1
AS 2501, *Auditing Accounting Estimates*	0	0	4
AS 2502, *Auditing Fair Value Measurements and Disclosures*	0	0	1
AS 2503, *Auditing Derivative Instruments, Hedging Activities, and Investments in Securities*	0	0	1
AS 2510, *Auditing Inventories*	0	1	1
AS 2801, *Subsequent Events*	0	0	1
AS 2810, *Evaluating Audit Results*	0	4	0

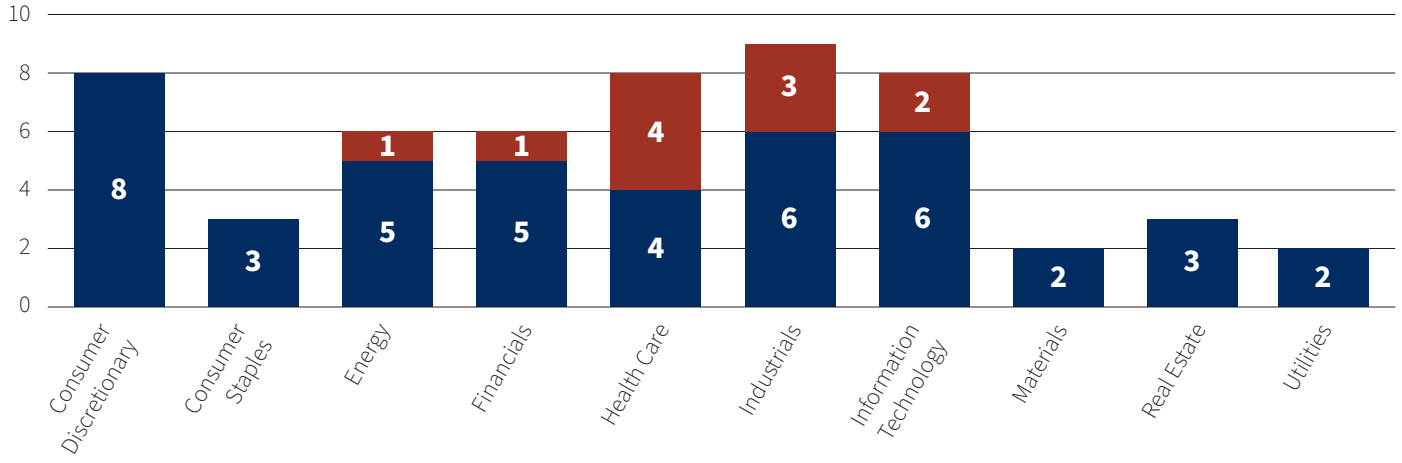
Inspection Results by Issuer Industry Sector

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 data for an issuer is not available from S&P, classifications are assigned based upon North American Industry Classification System data.

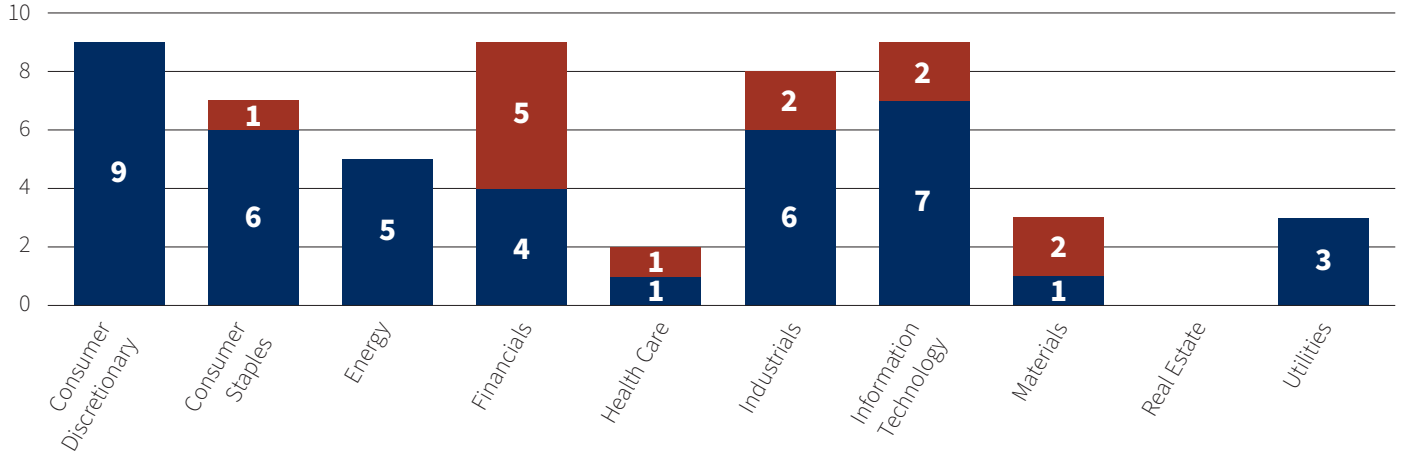
2018



2017



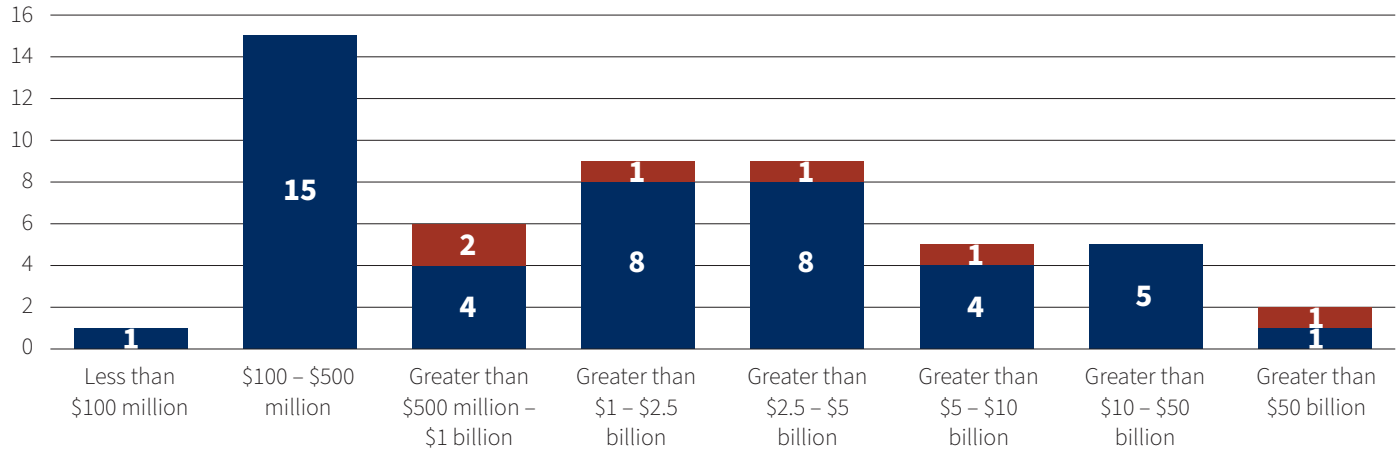
2016



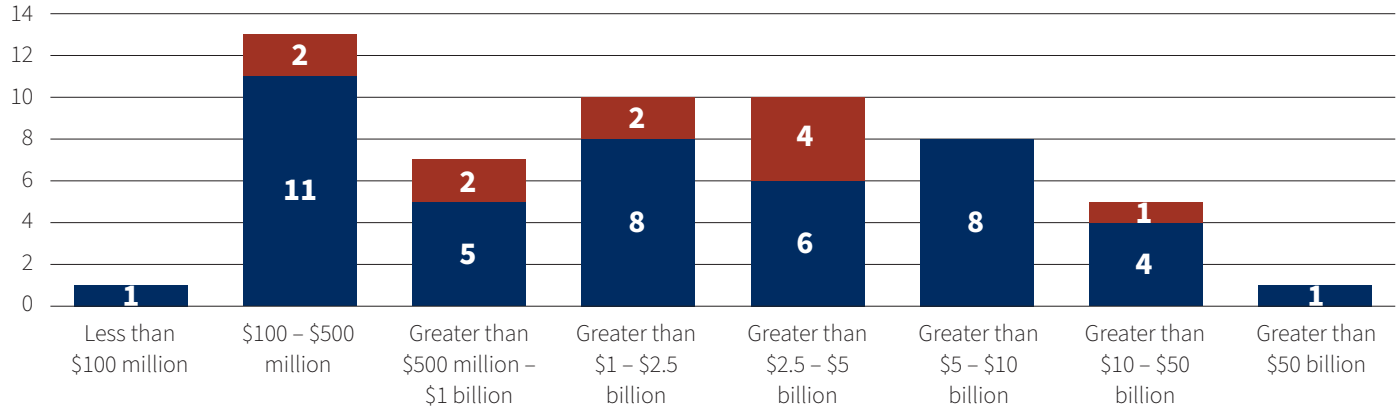
Audits without Part I.A deficiencies Audits with Part I.A deficiencies

Inspection Results by Issuer Revenue Range

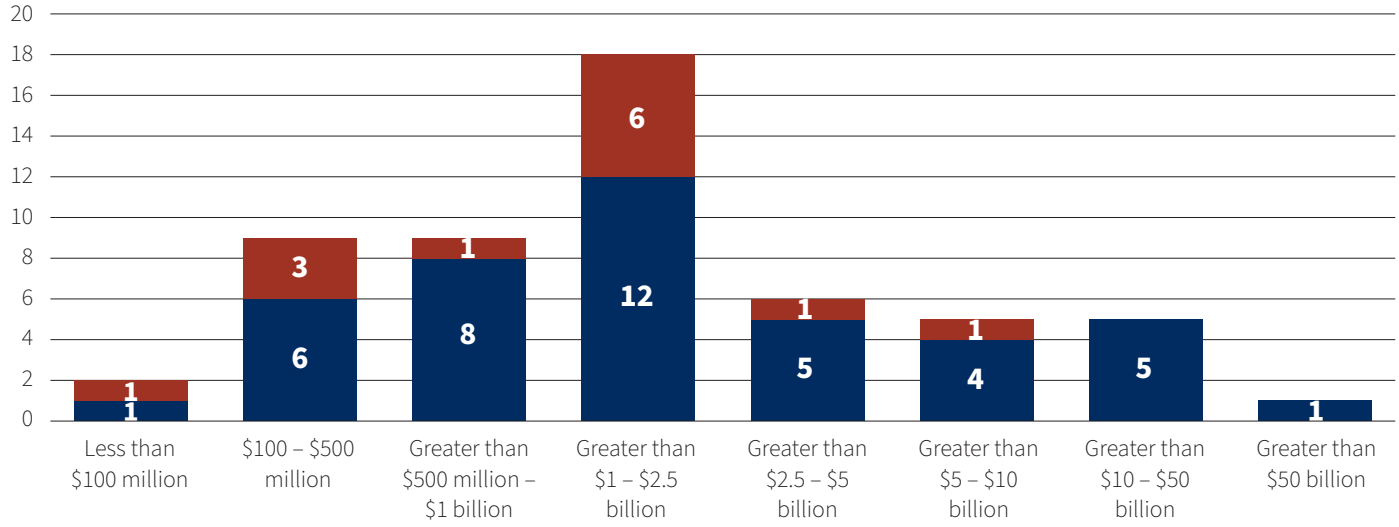
2018



2017



2016



Audits without Part I.A deficiencies Audits with Part I.A deficiencies

Classification of Audits with Part I.A Deficiencies

Within Part I.A of this report, we classify each issuer audit in one of the categories discussed below based on the Part I.A deficiency or deficiencies identified in our review.

The sole purpose of this classification system is to group and present issuer audits by the number of Part I.A deficiencies we identified within the audit as well as to highlight audits with an incorrect opinion on the financial statements and/or ICFR.

Audits with an Incorrect Opinion on the Financial Statements and/or ICFR

This classification includes instances where an audit deficiency was identified in connection with our inspection and, as a result, an issuer's financial statements were determined to be materially misstated, and the issuer restated its financial statements. It also includes instances where an audit deficiency was identified in connection with our inspection and, as a result, an issuer's ICFR was determined to be ineffective, or there were additional material weaknesses that the firm did not identify, and the firm withdrew its opinion, or modified its report, on ICFR.

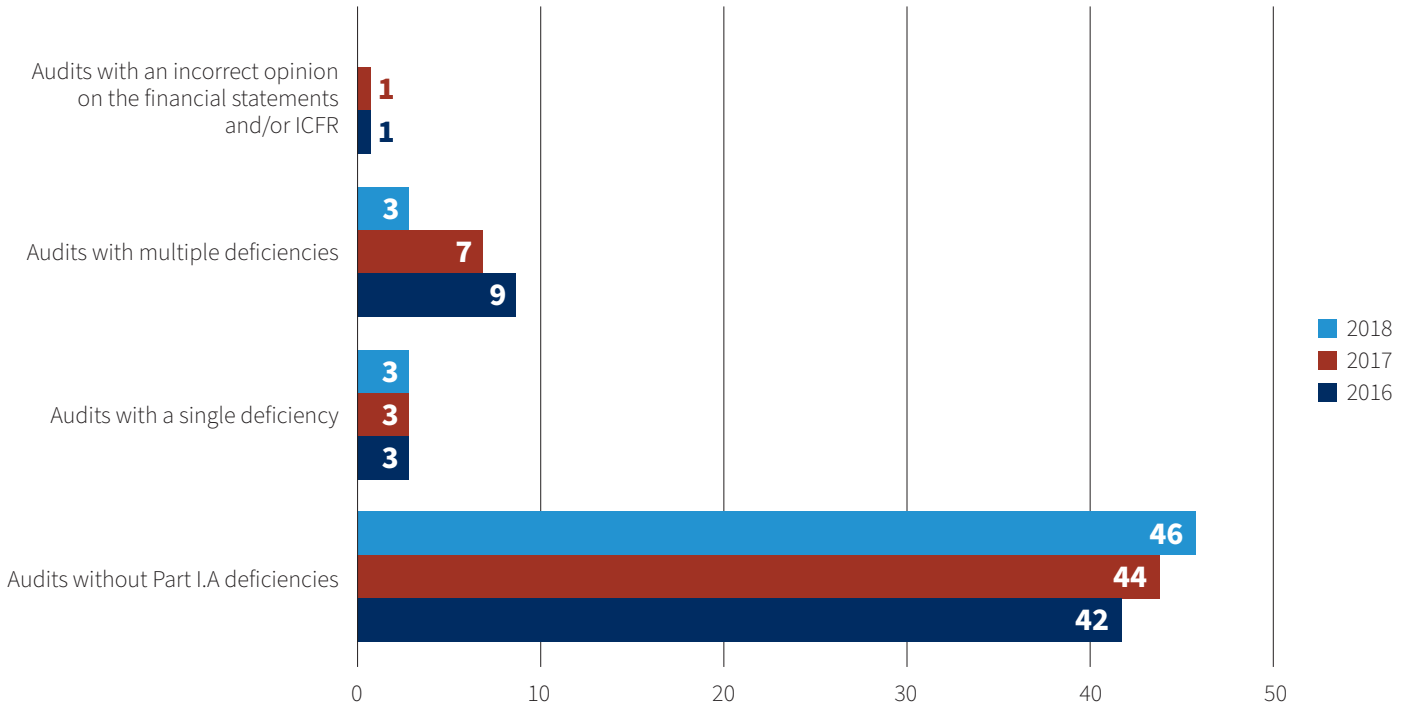
Audits with Multiple Deficiencies

This classification includes instances where multiple deficiencies were identified that related to a combination of one or more financial statement accounts, disclosures, and/or important controls in an ICFR audit.

Audits with a Single Deficiency

This classification includes instances where a single deficiency was identified that related to a financial statement account or disclosure or to an important control in an ICFR audit.

Number of Audits in Each Category



Part I: Inspection Observations

Part I.A of our report discusses deficiencies that were of such significance that we believe the firm, at the time it issued its audit report(s), had not obtained sufficient appropriate audit evidence to support its opinion on the issuer's financial statements and/or ICFR. Part I.B discusses deficiencies that do not relate directly to the sufficiency or appropriateness of evidence the firm obtained to support its opinion(s) but nevertheless relate to instances of non-compliance with PCAOB standards or rules. Consistent with the Act, it is the Board's assessment that nothing in Part I of this report deals with a criticism of or potential defect in the firm's quality control system. Any such criticisms or potential defects are discussed in Part II. Further, you should not infer from any Part I deficiency or combination of deficiencies that a quality control finding is identified in Part II.

Part I.A: Audits with Unsupported Opinions

This section of our report discusses the deficiencies identified, by specific issuer audit reviewed, in the audit work supporting the firm's opinion on the issuer's financial statements and/or ICFR.

We identify each issuer by a letter (e.g., Issuer A) and industry sector. Each deficiency could relate to several auditing standards, but we reference the PCAOB standard(s) that most directly relates to the requirement with which the firm did not comply.

Issuer audits are presented below within their respective deficiency classifications (as discussed previously). Within the classifications, we generally present the audits based on our assessment as to the relative significance of the identified deficiencies taking into account the significance of the financial statement accounts and/or disclosures affected, and/or the nature or extent of the deficiencies.

Audits with an Incorrect Opinion on the Financial Statements and/or ICFR

None

Audits with Multiple Deficiencies

Issuer A – Consumer Discretionary

Type of audit and related area affected

In our review, we identified deficiencies in the ICFR audit related to **Revenue**.

Description of the deficiencies identified

The issuer generated certain revenue at numerous locations from sales of multiple types of products. The firm selected for testing controls over this revenue that included (1) reviews of each location's monthly operating results and (2) reviews of monthly and year-to-date revenue for each type of product. The firm did not evaluate the specific review procedures that the control owners performed to evaluate whether the amounts recognized as revenue were appropriate. (AS 2201.42 and .44)

Issuer B – Industrials

Type of audit and related area affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Liabilities for Unpaid Insurance Claims**.

Description of the deficiencies identified

The issuer was self-insured for certain liabilities, and it used a service organization to administer the majority of the related claims. The claims data processed by this service organization were used to estimate the issuer's liabilities for unpaid insurance claims. The firm selected for testing a control over the accuracy of these claims data that consisted of claim audits performed by the service organization. The firm obtained the service auditor's report on the operating effectiveness of the service organization's controls but did not identify that the service auditor's testing of this control did not address the accuracy of the claims data. (AS 2201.B21)

The firm's approach for testing the liabilities for unpaid insurance claims was to develop an independent estimate. The firm did not perform substantive procedures to test, or (as discussed above) to sufficiently test controls over, the accuracy of claims data used in its independent estimate, beyond comparing a sample of claims from the service organization's claims processing system to claims data in the same system. (AS 1105.10)

Issuer C – Health Care

Type of audit and related area affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Liabilities for Self-Insurance Reserves**.

Description of the deficiencies identified

The issuer used claims activity reports to estimate its self-insurance reserves. The firm selected for testing a control that included a review of these claims activity reports for accuracy. The firm did not evaluate the specific procedures that the control owner performed to address the accuracy of certain data, including claims' incident dates, in the claims activity reports. (AS 2201.42 and .44)

The firm's approach for testing the self-insurance reserves was to develop an independent estimate. The firm did not perform substantive procedures to test, or (as discussed above) to sufficiently test controls over, the accuracy of claims' incident dates used in its independent estimate, beyond comparing the incident dates in the claims activity reports to the system that generated those reports. (AS 1105.10)

Audits with a Single Deficiency

Issuer D – Financials

Type of audit and related area affected

In our review, we identified a deficiency in the ICFR audit related to **Investments**.

Description of the deficiency identified

The firm selected for testing a control over the valuation of certain investments that consisted of the review of analyses and memoranda summarizing established fair values. The firm did not evaluate the review procedures that the control owners performed, including the criteria that the control owners used to identify items for follow up and whether those items were appropriately resolved. (AS 2201.42 and .44)

Issuer E – Health Care

Type of audit and related area affected

In our review, we identified a deficiency in the ICFR audit related to **Liabilities for Incurred But Not Reported Claims**.

Description of the deficiency identified

The issuer used historical claims data to estimate the liabilities for incurred but not reported claims. These data consisted of numerous loss triangles that included monthly historical claims incurred and claims adjudicated or paid for multiple periods. For one of the issuer's reporting segments, the firm selected for testing an automated application control over the generation of reports containing historical claims data. The firm did not test the configuration of the automated control or perform other procedures that would have provided sufficient appropriate audit evidence that the automated control was designed and operating effectively. (AS 2201.42, .44, and .B9)

Issuer F – Financials

Type of audit and related area affected

In our review, we identified a deficiency in the financial statement audit related to **Deposit Liabilities**.

Description of the deficiency identified

The firm sent positive confirmation requests to the issuer's customers for a sample of deposit liabilities. For the items in its sample for which the requested confirmations were not returned, the firm did not perform alternative procedures that provided sufficient evidence that the recorded amounts of the deposit liabilities were accurate as of the confirmation date. (AS 2310.31)

Part I.B: Other Instances of Non-Compliance with PCAOB Standards or Rules

This section of our report discusses any deficiencies we identified that do not relate directly to the sufficiency or appropriateness of evidence the firm obtained to support its opinion(s) but nevertheless relate to instances of non-compliance with PCAOB standards or rules. When we review an audit, we do not review every aspect of the audit. As a result, the areas below were not reviewed on every audit inspected.

The deficiencies below are presented in numerical order based on the PCAOB standard or rule with which the firm did not comply. We identified the following deficiencies:

- In 13 of 52 audits reviewed, the firm did not include all relevant work papers in the final set of audit documentation it was required to assemble. In these instances, the firm was non-compliant with AS 1215, *Audit Documentation*.
- In eight of 26 audits reviewed where one or more other accounting firms participated in the firm's audit, the firm's report on Form AP omitted information related to the participation in the audit by certain other accounting firms that was required to be reported. In these instances, the firm was non-compliant with PCAOB Rule 3211, *Auditor Reporting of Certain Audit Participants*.

Part II: Observations Related To Quality Control

Part II of our report discusses criticisms of, and potential defects in, the firm's system of quality control.

Deficiencies are included in Part II if an analysis of the inspection results, including the results of the reviews of individual audits, indicates that the firm's system of quality control does not provide reasonable assurance that firm personnel will comply with applicable professional standards and requirements. Generally, the report's description of quality control criticisms is based on observations from our inspection procedures.

Any changes or improvements to its system of quality control that the firm may have brought to the Board's attention may not be reflected in this report, but are taken into account during the Board's assessment of whether the firm has satisfactorily addressed the quality control criticisms or defects no later than 12 months after the issuance of this report.

Criticisms of, and potential defects in, the firm's system of quality control, to the extent any are identified, are nonpublic when the reports are issued. If a firm does not address to the Board's satisfaction any criticism of, or potential defect in, the firm's system of quality control within 12 months after the issuance of our report, any such deficiency will be made public.

Appendix A: Firm's Response to the 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, excluding any portion granted confidential treatment, is attached hereto and made part of this final inspection report.

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. 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.

Deloitte.

30 Rockefeller Plaza
New York, NY 10112
USA

March 20, 2020

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 2018 Inspection (PUBLIC)

Dear Mr. Botic:

Deloitte & Touche LLP is pleased to submit this response to the draft Report on the 2018 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,

Lara Abrash
Chairman and Chief Executive Officer
Deloitte & Touche LLP

Joseph B. Ucuzoglu
Chief Executive Officer
Deloitte

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