Inspection of
Demetrius & Company, L.L.C.

Issued by the
Public Company Accounting Oversight Board

May 21, 2008

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
Notes Concerning this Report

1. Portions of this report may describe deficiencies or potential deficiencies in the systems, policies, procedures, practices, or conduct of the firm that is the subject of this report. The express inclusion of certain deficiencies and potential deficiencies, however, should not be construed to support any negative inference that any other aspect of the firm's systems, policies, procedures, practices, or conduct is approved or condoned by the Board or judged by the Board to comply with laws, rules, and professional standards.

2. Any references in this report to violations or potential violations of law, rules, or professional standards should be understood in the supervisory context in which this report was prepared. Any such references are not a result of an adversarial adjudicative process and do not constitute conclusive findings of fact or of violations for purposes of imposing legal liability. Similarly, any description herein of a firm's cooperation in addressing issues constructively should not be construed, and is not construed by the Board, as an admission, for purposes of potential legal liability, of any violation.

3. Board inspections encompass, among other things, whether the firm has failed to identify departures from U.S. Generally Accepted Accounting Principles ("GAAP") or Securities and Exchange Commission ("SEC" or "Commission") disclosure requirements in its audits of financial statements. This report's descriptions of any such auditing failures necessarily involve descriptions of the related GAAP or disclosure departures. The Board, however, has no authority to prescribe the form or content of an issuer's financial statements. That authority, and the authority to make binding determinations concerning an issuer's compliance with GAAP or Commission disclosure requirements, rests with the Commission. Any description, in this report, of perceived departures from GAAP or Commission disclosure requirements should not be understood as an indication that the Commission has considered or made any determination regarding these issues unless otherwise expressly stated.
INSPECTION OF DEMETRIUS & COMPANY, L.L.C.

The Public Company Accounting Oversight Board ("PCAOB" or "the Board") has conducted an inspection of the registered public accounting firm Demetrius & Company, L.L.C. ("the Firm"). The Board is issuing this report of that inspection in accordance with the requirements of the Sarbanes-Oxley Act of 2002 ("the Act").

The Board is making portions of the report publicly available. Specifically, the Board is releasing to the public Part I of the report and portions of Part IV of the report. Part IV of the report consists of the Firm's comments, if any, on a draft of the report.1/

The Board has elsewhere described in detail its approach to making inspection-related information publicly available consistent with legal restrictions.2/ A substantial portion of the Board's criticisms of a firm (specifically criticisms of the firm's quality control system), and the Board's dialogue with the firm about those criticisms, occurs out of public view, unless the firm fails to make progress to the Board's satisfaction in addressing those criticisms. In addition, the Board generally does not disclose otherwise nonpublic information, learned through inspections, about the firm or its clients. Accordingly, information in those categories generally does not appear in the publicly available portion of an inspection report.

1/ 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 addition, pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(b), if a firm requests, and the Board grants, confidential treatment for any of the firm's comments on a draft report, the Board does not include those comments in the final report at all. The Board routinely grants confidential treatment, if requested, for any portion of a firm's response that addresses any point in the draft that the Board omits from, or any inaccurate statement in the draft that the Board corrects in, the final report.

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's inspection staff ("the inspection team") conducted fieldwork for the inspection from July 10, 2006 to July 14, 2006 and on July 20, 2006 and July 28, 2006. The fieldwork included procedures tailored to the nature of the Firm, certain aspects of which the inspection team understood at the outset of the inspection to be as follows:

- Number of offices: 1 (Wayne, New Jersey)
- Ownership structure: Limited liability company
- Number of partners: 5
- Number of professional staff: 8
- Number of issuer audit clients: 16

Board inspections are designed to identify and address weaknesses and deficiencies related to how a firm conducts audits. To achieve that goal, Board inspections

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3/ "Professional staff" includes all personnel of the Firm, except partners or shareholders and administrative support personnel. The number of partners and professional staff is provided here as an indication of the size of the Firm, and does not necessarily represent the number of the Firm's professionals who participate in audits of issuers or are "associated persons" (as defined in the Act) of the Firm.

4/ The number of issuer audit clients shown here is based on the Firm's self-reporting and the inspection team's review of certain information for inspection planning purposes. It does not reflect any Board determination concerning which, or how many, of the Firm's audit clients are "issuers" as defined in the Act. In some circumstances, a Board inspection may include a review of a firm's audit of financial statements of an issuer that ceased to be an audit client before the inspection, and any such former clients are not included in the number shown here.

5/ This focus necessarily carries through to reports on inspections and, accordingly, Board inspection reports are not intended to serve as balanced report cards or overall rating tools.
inspections include reviews of certain aspects of selected audits performed by the firm and reviews of other matters related to the firm's quality control system.

In the course of reviewing aspects of selected audits, an inspection may identify ways in which a particular audit is deficient, including failures by the firm to identify, or to address appropriately, respects in which an issuer’s financial statements do not present fairly the financial position, results of operations, or cash flows of the issuer in conformity with GAAP.\textsuperscript{6} It is not the purpose of an inspection, however, to review all of a firm's audits or to identify every respect in which a reviewed audit is deficient. Accordingly, a Board inspection report should not be understood to provide any assurance that the firm's audits, or its issuer clients' financial statements, are free of any deficiencies not specifically described in an inspection report.

A. Review of Audit Engagements

The inspection procedures included a review of aspects of the Firm's auditing of financial statements of six issuers. The scope of this review was determined according to the Board's criteria, and the Firm was not allowed an opportunity to limit or influence the scope.

The inspection team identified what it considered to be audit deficiencies.\textsuperscript{7} The deficiencies identified in three of the audits reviewed included deficiencies of such significance that it appeared to the inspection team that the Firm did not obtain sufficient

\textsuperscript{6} 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 GAAP, the Board's practice is to report that information to the SEC, which has jurisdiction to determine proper accounting in issuers' financial statements.

\textsuperscript{7} PCAOB standards require a firm to take appropriate actions to assess the importance of audit deficiencies identified after the date of the audit report to the firm's present ability to support its previously expressed opinions. See AU 390, Consideration of Omitted Procedures After the Report Date, and AU 561, Subsequent Discovery of Facts Existing at the Date of the Auditor's Report (both included among the PCAOB's interim auditing standards, pursuant to PCAOB Rule 3200T). Failure to comply with these PCAOB standards could be a basis for Board disciplinary sanctions.
compotent evidential matter to support its opinion on the issuer's financial statements. Those deficiencies were –

(1) the failure, in two engagements, to perform sufficient audit procedures to evaluate the accounting for the issuance of equity instruments, including, in one case, the failure to evaluate the appropriateness of recording the issuance of certain equity instruments as a prepaid expense;

(2) the failure to perform procedures to obtain an understanding of the methods and assumptions used by a specialist and to test data provided to the specialist in the valuation of investment securities; and

(3) the failure to perform procedures to test sales and servicing rights of mortgage loans.

B. Review of Quality Control System

In addition to evaluating the quality of the audit work performed on specific audits, the inspection included review of certain of the Firm's practices, policies, and procedures related to audit quality. This review addressed practices, policies, and procedures concerning audit performance, training, compliance with independence standards, client acceptance and retention, and the establishment of policies and procedures. As described above, any defects in, or criticisms of, the Firm’s quality control system are discussed in the nonpublic portion of this report and will remain

\[8/\] In some cases, an inspection team's observation that a firm failed to perform a procedure may be based on the absence of documentation and the absence of persuasive other evidence, even if a firm claims to have performed the procedure. PCAOB Auditing Standard No. 3, *Audit Documentation*, ("AS No. 3") 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. See AS No. 3, paragraph 9; Appendix A to AS No. 3, paragraph A28. For purposes of the inspection, an observation that the Firm did not perform a procedure, obtain evidence, or reach an appropriate conclusion may be based on the absence of such documentation and the absence of persuasive other evidence.
nonpublic unless the Firm fails to address them to the Board's satisfaction within 12 months of the date of this report.

END OF PART I
PART II

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B. Issues Related to Quality Controls

The inspection of the Firm included consideration of aspects of the Firm's system of quality control. Assessment of a firm's quality control system rests both on review of a firm's stated quality control policies and procedures and on inferences that can be drawn from respects in which a firm's system has failed to assure quality in the actual performance of engagements. On the basis of the information reported by the inspection team, the Board has the following concerns about aspects of the Firm's system of quality control.

* * * *

2. Audit Performance

A firm's system of quality control should provide reasonable assurance that the work performed on an audit engagement will meet applicable professional standards and regulatory requirements. On the basis of the information reported by the inspection team, including the audit performance deficiencies described in Part II.A and any other deficiencies identified below, the Board has concerns that the Firm's system of quality control fails to provide such reasonable assurance in at least the following respects –

a. Technical Competence, Due Care, and Professional Skepticism

The Firm's system of quality control appears not to do enough to ensure technical competence and the exercise of due care or professional skepticism.

* * * *

9/ A firm's failure to comply with the requirements of PCAOB standards when performing an audit may be an indication of a potentially significant defect in a firm's quality control system even if that failure did not result in an insufficiently supported audit opinion.
d. Concurring Partner Review

Questions exist about the effectiveness of the Firm’s existing arrangement for concurring partner reviews. Having procedures for concurring partner review by a competent reviewer is an important element of quality control. Such reviews should involve the performance of appropriate procedures using due care and professional skepticism, with the Firm appropriately addressing the reviewer's findings and documenting the process. The information reported by the inspection team suggests that there is no evidence that the concurring partner review procedure used by the Firm resulted in the identification of any of the deficiencies noted by the inspection team. Apparent deficiencies in documentation of the scope and results of the concurring partners' reviews make it difficult to identify the principal cause of the problem, but potential causes include a lack of competency, due care or professional skepticism on the part of the concurring partners; deficiencies in the scope of the concurring partners' procedures; and/or the Firm's failure to properly address the concurring partners' findings.

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PART IV

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.

\[\text{In any version of this report that the Board makes publicly available, any portions of the Firm's response that address nonpublic portions of the report are omitted unless a firm specifically requests otherwise. In some cases, the result may be that none of a firm's response is made publicly available.}\]
September 25, 2007

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

Re: Response to the Public Company Accounting Oversight Board

Dear Mr. Diacont:

We are pleased to provide this response to the Public Company Accounting Oversight Board's (the "PCAOB" or the "Board") draft report (the Report) on the initial inspection of Demetrius & Company, L.L.C. ("Demetrius," or "Firm"), performed during 2008. We believe that the PCAOB and Demetrius & Company, L.L.C. share a mutual objective to continually improve audit quality. Approximately one year ago, the PCAOB inspection team performed their initial inspection of our Firm, covering audit years ended June 30, 2004 and 2005 and December 31, 2005 of issuers and existing Firm policies. We responded quickly with audit enhancements for use on the December 31, 2005 audits to address the preliminary comments we received. As the PCAOB focuses on different areas in its inspections, as auditing standards change and as best practices evolve, we believe that our Firm and the entire audit profession will experience continual improvement in audit quality.

Each of the specific matters noted in Part I of the Report have been addressed by appropriate action where in our professional judgment it was required. We have also considered whether it was necessary to perform additional procedures in accordance with AU 390, Consideration of Omitted Procedures After the Report Date, and AU 561, Subsequent Discovery of Facts Existing at the Date of the Auditor's Report. As a result, we either enhanced our documentation in the work papers or performed some additional procedures. No facts or circumstances came to our attention during the inspection or in preparing this response to the Report which caused us to believe that any of our previously issued reports should be withdrawn.

The Report comments reflect differences between judgments made by audit engagement teams during the real-time process of the audit and those of inspectors during an inspection performed after such audits were completed. Our audit philosophy has been principles-based with emphasis on use of professional judgment, and application of professional judgment is required in many decisions in every audit. The audit inspection process necessarily involves evaluation of those judgments and may result in differing views on certain judgments made during the conduct of an audit.

We appreciate the opportunity to provide this response and look forward to further dialogue with the Board's Inspections Staff or the Board about enhancing audit quality and improvements to the auditing profession.

Sincerely,

Demetrius & Company, L.L.C.

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A PCAOB REGISTERED FIRM
Mr. George Diacont
Director
Division of Registration and Inspections
Public Company Accounting Oversight Board
1666 K Street NW
Washington, DC 2006

Re: Response to the Public Company Accounting Oversight Board

Dear Mr. Diacont:

This constitutes Demetrius & Company, L.L.C.'s detailed response to Part II of the draft report on the initial inspection of our firm performed during 2006.

REDACTED. Comments on Non-public Aspects of Report
NON-PUBLIC RESPONSE

REDACTED: Comments on Non-public Aspects of Report

B. Issues Related to Quality Control

We believe the Board’s assessment of our system of quality control over issuers to be unfair. In our professional judgment regarding the issuers reviewed, we obtained sufficient competent evidential matter to support our auditors’ opinion. In some instances there was a lack of understanding of the transactions by the inspectors. As previously stated we take issue with the majority of the comments in the draft report. Our firm has an outstanding reputation for quality among our peers. Many of which use us as a resource for accounting and auditing matters. It is our opinion that our system of quality control over issuers gives reasonable assurance of complying with professional standards. Absolute assurance is not obtainable in the real world. For a firm of our size we have spent a lot of time and money to be the best in our class. The following addresses each of the Board’s quality control concerns:

REDACTED: Comments on Non-public Aspects of Report

2. Audit Performance
   a. Technical Competence, Due and Professional Skepticism

We take issue with the Board. The firm has two partners with 100 years of audit experience, including issuers work, between them, much with major international firms. Also our quality control manager has over 40 years experience, and an audit partner with two major firms before retiring. All work performed not reviewed by a manager or in-charge associate is reviewed by the lead partner, sometimes with the assistance of the QC manager. All of our professional staff receives at least 120 hours of continuing professional education (CPE) every three years in
subjects relating to our practice, with heavy emphasis on current standards. We attend
conferences on SEC, PCAOB, and FASB. These courses are sponsored by FAE of NYSSCPA,
NJSCPA, AICPA and the firm. Most of the firm’s sponsored programs were video programs from
the AICPA and their various WEB based programs. Some of the seminars attended during the
CPE year ended August 31, 2006 included: Banking conference, Derivatives Embedded
Warrants and Options, Independence training, Fraud in the Governmental and not-for-profit
Environment; Sarbanes, Oxley Act, SEC, PCAOB and Conference, Accounting for Stock Options
and other Stock-Based Compensation and Constructions Contractors, Accounting, Consulting
and Taxation. All associates are required to take the NJSCPA two day Staff Training Courses;
Level I, Level II and Level III. Many video presentations have a partner or manager as a
discussion leader. Our senior partners always inject their war stories from their many years of
auditing. All our CPA’s are qualified captains or reviewers on peer reviews in all programs. We
also act as concurring reviewers and consultants for many other accounting firms.

In addition, our research resources consist of on-line research service for all accounting, auditing
and SEC literatures. A library contains hundreds of recently issued annual reports of issuers.
The firm subscribes on-line to 10-K Wizard. Also, we download recent inspection reports from
the PCAOB’s home pages and disseminate to staff. We are a member of “shared professional
services” of one of the 10 largest accounting firms and as result receive by e-mail all their staff
bulletins. These are forwarded to our partners and staff. As an alumni of a big four firm we also
receive by e-mail their commentaries on current accounting and auditing issues.

d. Concurring Partner Review

We believe our concurring reviewers have the competency required by professional standards.
Concurring partners are all lead partners on other audits. Again this is an area of judgment on
what matters may cause the auditors’ report and the related financial statements to be materially
misleading. Our concurring partners do review key workpapers. We do agree that our concurring
review process can be improved. Accordingly, we are rethinking in on the focus and
documentation of the whole concurring review process.

In closing, although we do not agree with all the inspection teams’ findings, we are
committed to improving the quality of our audits and the documentation thereof. We have always
put quality of our product above profits. All our partners, managers and staff are fully aware of
our emphasis on quality from the day they join us and forward.
NON - PUBLIC RESPONSE

We appreciate this opportunity to provide you our response and look forward to further dialogue on the most effective means of enhancing audit quality. If you have any questions regarding this letter, please contact John A. Demetrius at 973-812-0100, extension 200.

Sincerely,

Demetrius & Company, L.L.P.