

Report on
2012 Inspection of Grant Thornton LLP
(Headquartered in Chicago, Illinois)

Issued by the
Public Company Accounting Oversight Board

November 21, 2013

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**

2012 INSPECTION OF GRANT THORNTON LLP

Preface

In 2012, the Public Company Accounting Oversight Board ("PCAOB" or "the Board") conducted an inspection of the registered public accounting firm Grant Thornton LLP ("the Firm") pursuant to the Sarbanes-Oxley Act of 2002 ("the Act").^{1/}

The inspection process is designed, and inspections are performed, to provide a basis for assessing the degree of compliance by a firm with applicable requirements related to auditing issuers. The inspection process included reviews of aspects of selected issuer audits completed by the Firm. The reviews were intended to identify whether deficiencies existed in those aspects of the audits, and whether such deficiencies indicated defects in the Firm's system of quality control over audits. In addition, the inspection included reviews of policies and procedures related to certain quality control processes of the Firm that could be expected to affect audit quality.

The issuer audits and aspects of those audits inspected were selected based on a number of risk-related and other factors. Due to the selection process, the deficiencies included in this report are not necessarily representative of the Firm's issuer audit practice.

The Board is issuing this report in accordance with the requirements of the Act.^{2/} The Board is releasing to the public Part I of the report and portions of Appendix C. Appendix C includes the Firm's comments, if any, on a draft of the report. Any defects in, or criticisms of, the Firm's quality control system are discussed in the nonpublic portion of this report and will remain nonpublic unless the Firm fails to address them to the Board's satisfaction within 12 months of the date of this report.

^{1/} The Act requires the Board to conduct an annual inspection of each registered public accounting firm that regularly provides audit reports for more than 100 issuers.

^{2/} In its *Statement Concerning the Issuance of Inspection Reports*, PCAOB Release No. 104-2004-001 (August 26, 2004), the Board described its approach to making inspection-related information publicly available consistent with legal restrictions.

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's staff ("the inspection team") conducted primary procedures for the inspection from June 2012 through March 2013. The inspection team performed field work at the Firm's National Office and at 18 of its approximately 55 U.S. practice offices.

A. Review of Audit Engagements

The 2012 inspection of the Firm included reviews of aspects of 34 audits performed by the Firm. The inspection team identified matters that it considered to be deficiencies in the performance of the work it reviewed. One of the deficiencies relates to auditing aspects of an issuer's financial statements that the issuer restated after the primary inspection procedures.^{3/}

The inspection team considered certain of the deficiencies that it observed to be audit failures. As used in PCAOB inspection reports, the term "audit failure" refers to an audit in which the inspection team identified one or more deficiencies that were of such significance that it appeared that the Firm, at the time it issued its audit report, had failed to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements and/or on the effectiveness of internal control over financial reporting ("ICFR"). The audit deficiencies that reached this level of significance are described below.^{4/}

^{3/} The Board's inspection process did not include review of any additional audit work related to the restatement.

^{4/} The discussion in this report of any deficiency observed in a particular audit reflects information reported to the Board by the inspection team and does not reflect any determination by the Board as to whether the Firm has engaged in any conduct for which it could be sanctioned through the Board's disciplinary process. In addition, any references in this report to violations or potential violations of law, rules, or professional standards are not a result of an adversarial adjudicative process and do not constitute conclusive findings for purposes of imposing legal liability.

A.1. Issuer A

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

- The Firm failed to identify a departure from generally accepted accounting principles ("GAAP") that it should have identified and addressed before issuing its audit opinion. Specifically, the issuer accounted for its interest-rate swap agreements as hedges, and recorded changes in the fair value of these agreements in accumulated other comprehensive income, without complying with the hedging provisions of Financial Accounting Standards Board Accounting Standards Codification Topic 815, *Derivatives and Hedging*.
- The Firm's procedures to test controls related to property, plant, and equipment ("PP&E") were insufficient. Specifically –
 - The Firm failed to sufficiently test a review control over the progress of capital projects, as its procedures were limited to observing evidence that participants were invited to a meeting where the review would be performed. The Firm failed to evaluate whether the control was designed and operated at a level of precision that would prevent or detect material misstatements related to PP&E.
 - The Firm failed to test the accuracy and completeness of the list of additions to PP&E that it used when testing a control over the approval of capital projects.
- The Firm failed to perform sufficient substantive procedures to test PP&E, as it designed its procedures based on a level of reliance on controls that was excessive due to the deficiencies in the Firm's testing of controls discussed above. As a result, the sample size the Firm used to test additions to PP&E was insufficient to obtain the necessary level of assurance. In addition, the sample the Firm selected for testing included items that represented project transfers, which were not current-year

additions to PP&E, but the Firm failed to make alternative selections for these items.

- The Firm failed to perform sufficient procedures to test revenue related to a government subsidy program. Specifically, the Firm failed to identify and test any controls over the issuer's compliance with regulations governing participation in the subsidy program, and the Firm's substantive procedures to test this revenue were limited to obtaining written representations from management that it was not aware of any violations of the regulations.

A.2. Issuer B

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

- The Firm failed to identify and test any controls over the development of the cash flow projections the issuer used in determining the amount and timing of finance income from acquired accounts receivable and the valuation of those accounts receivable.
- The Firm's testing of a review control over the quarterly impairment analysis for acquired accounts receivable was not sufficient. Specifically, the Firm limited its testing to holding discussions with management and observing evidence that reviews that were part of the operation of the control had occurred, without evaluating whether the control operated at a level of precision that would prevent or detect material misstatements.
- The issuer calculated the amortization of finance income using a software tool and then transferred the relevant amounts to a database within the issuer's systems. The Firm failed to test any controls over the accuracy and completeness of the amounts transferred to the database.
- The Firm selected for testing a control over the recording of cash collections and stated that it tested this control as part of its substantive procedures. The Firm, however, failed to test, through any of its

procedures, whether the control operated at a level of precision that would prevent or detect material misstatements related to cash collections.

- The issuer used cash flow projections, which were based in part on projections provided by multiple external parties that serviced portions of the portfolio, to evaluate the majority of acquired accounts receivable for possible impairment. The Firm failed to evaluate the reasonableness of an important assumption the issuer used in the cash flow projections, beyond noting that the external parties used, for this assumption, rates that were generally consistent with each other. The Firm did not take into account that the issuer's assumption was not consistent with historical results.
- The Firm failed to sufficiently evaluate the reasonableness of certain assumptions the issuer used in projecting future taxable income for the purposes of its analysis of the valuation of deferred tax assets. Specifically, there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had taken into account certain available information that appeared inconsistent with the issuer's assumptions relating to the forecasted level of acquisitions of accounts receivable portfolios and projected impairments of accounts receivable.

A.3. Issuer C

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

- The Firm failed to sufficiently test controls over revenue. Specifically, the Firm limited its procedures in this area to testing controls over whether cash and credit card receipts were appropriately recorded to the issuer's cash accounts, but it failed to test any controls over the recording of revenue.
- The Firm failed to perform sufficient procedures to test controls over the cost of goods sold in the sales transactions the issuer recorded, as the control the Firm selected for testing related only to the existence of rental inventory.

- The Firm failed to test any controls over the reconciliation of the rental merchandise subsidiary ledger to the general ledger.
- The issuer's system calculated depreciation expense for rental merchandise based on rental income projections. The Firm failed to test any controls over the development of the underlying assumptions or the reasonableness of the projections.
- The Firm failed to perform sufficient substantive procedures to test revenue. Specifically –
 - The Firm's substantive procedures to test revenue were limited to testing whether cash and credit card receipts were appropriately recorded to the issuer's cash accounts, without testing the recording of revenue.
 - The Firm failed to perform procedures to test whether certain transactions met the criteria to be accounted for using the installment method of accounting.
- The Firm failed to test the existence of accounts receivable from installment sales.
- The Firm failed to perform sufficient substantive procedures to test the valuation of rental merchandise. Specifically –
 - The Firm calculated its sample size for price testing based on a "significant" level of assurance provided by analytical procedures it performed; however, because of the deficiencies in the analytical procedures noted below, they provided little to no substantive assurance. As a result, the Firm's sample size was insufficient.

With respect to the analytical procedures, the Firm established thresholds for investigating variances; however, the Firm set the thresholds at a level that would have allowed the Firm not to identify individual variances that may be potential material misstatements. Further, the Firm failed to perform procedures to

obtain corroboration of explanations provided by management for certain differences in excess of its established thresholds.

- The Firm failed to perform sufficient procedures to test depreciation expense for rental merchandise, as its procedures were limited to the analytical procedures noted above.
- The Firm failed to test the accuracy of certain data included in a report that it used to evaluate the reasonableness of a reserve for idle rental merchandise.
- The Firm failed to perform sufficient testing of the cost of goods sold in the sales transactions the issuer recorded during the first nine months of the year, as its procedures were limited to testing the existence of rental merchandise inventory and performing the analytical procedures noted above.

A.4. Issuer D

In this audit, in addition to the deficiencies described in Part I.A.23 related to testing the fair value measurements of, and disclosures related to, financial instruments without readily determinable fair values ("hard-to-value financial instruments"), the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and on the effectiveness of ICFR –

- The Firm's procedures to test certain review controls over the identification and assessment of variable interest entities ("VIEs") and the valuation of the allowance for loan losses ("ALL"), available-for-sale real estate securities, and bonds payable were insufficient. Specifically –
 - The Firm used the work of the issuer's internal auditors as evidence regarding the effectiveness of the review control over the identification and assessment of VIEs. The Firm, however, failed to perform any testing of its own.
 - The procedures to test the review controls over VIEs and the other areas noted above were limited to observing evidence that reviews

had occurred, without testing whether the controls operated at a level of precision that would prevent or detect material misstatements related to these areas.

- The Firm failed to perform sufficient substantive procedures to test the identification and assessment of VIEs. Specifically, the Firm failed to test whether the issuer had identified all investments that required an assessment to determine whether the investments met the criteria to be considered VIEs. In addition, as the Firm limited its testing of VIEs to those investments the issuer had determined were VIEs, it failed to test the appropriateness of the issuer's conclusions related to those investments the issuer had determined were not VIEs.
- The Firm failed to perform sufficient substantive procedures to test the ALL. Specifically –
 - For certain collateral-dependent loans, the issuer determined the ALL based on estimated discounted cash flows from the real estate that served as collateral for the loans. The Firm failed to sufficiently evaluate the reasonableness of certain assumptions the issuer used in its discounted cash-flow analyses, as follows –
 - The Firm limited its evaluation of the issuer's discount and capitalization rate assumptions to comparing those rates to published industry data. The Firm, however, failed to determine whether the industry data correlated to the real estate underlying the loans. In addition, in one instance, the discount rate the issuer used fell outside the relevant range, but the Firm performed no additional procedures to address this inconsistency.
 - The Firm's evaluation of cash flow projections for certain of these loans was limited to noting the expected growth for the U.S. economy and inquiring of management regarding differences between historical information and the first-year projections, and the Firm failed to take into account certain

current operating results that appeared inconsistent with some of the assumptions used in the projections.

- The Firm failed to sufficiently test the completeness of the population of loans the issuer evaluated for possible impairment. Specifically, the Firm selected for testing loans that the issuer did not evaluate for possible impairment, but the Firm's assessment of certain risk factors related to those loans was limited to inquiry of management.

A.5. Issuer E

In this audit, in addition to the deficiencies described in Part I.A.23 related to testing the fair value measurements of, and disclosures related to, hard-to-value financial instruments, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and on the effectiveness of ICFR –

- The Firm's procedures to test controls over the valuation of investment securities, the ALL, and goodwill were insufficient. Specifically –
 - The Firm selected for testing only one control, a review control, over the valuation of investment securities. The Firm's procedures to test this control were limited to observing evidence that the review had occurred, without evaluating whether the control operated at a level of precision that would prevent or detect material misstatements related to the valuation of investment securities.
 - The Firm failed to perform direct testing of certain review controls over the ALL that it had selected. For one control, consisting of management's review of the ALL, the Firm stated that its substantive procedures provided evidence of the operating effectiveness of the control. For another control, consisting of management's review of schedules supporting the ALL, the Firm selected samples of loans and recalculated the aging of the loans or compared its risk rating of the loans to the issuer's risk rating.

The Firm's procedures did not constitute direct testing of these controls.

- The Firm failed to test any controls over the issuer's analysis of the possible impairment of goodwill.
- The Firm failed to perform sufficient substantive procedures to test the ALL. Specifically –
 - To test the issuer's loan risk-rating process, which the issuer used to determine important inputs to the ALL calculation, the Firm selected loans for testing that exceeded a monetary threshold and also selected the largest loans that met certain risk-related criteria. The Firm failed to perform any procedures to test the loans excluded from this test, which represented nearly 90 percent of the loan balance.
 - The Firm failed to evaluate the reasonableness of important assumptions the issuer used to calculate the general reserve component of the ALL.
 - The Firm failed to perform procedures to determine that all of the loans that required evaluation for possible impairment were evaluated.

A.6. Issuer F

In this audit, in addition to the deficiencies described in Part I.A.23 related to testing the fair value measurements of hard-to-value financial instruments, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and on the effectiveness of ICFR –

- The Firm selected for testing certain review controls over the valuation of real estate securities and the ALL; however, the testing of these controls was insufficient. Specifically –

- The Firm identified a fraud risk for a significant component of the ALL. The Firm, however, used the work of internal audit as its evidence of the operating effectiveness of an important review control over the ALL without performing any of its own testing of this review control.
- The testing of the ALL review control and of the other review controls referenced above was limited to observing evidence of management's review and approval, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements related to these areas.
- The Firm failed to perform sufficient substantive procedures to test the ALL. Specifically, there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had –
 - Performed sufficient procedures to evaluate the reasonableness of an assumption related to the timing of future loan losses that the issuer used in calculating the ALL. Specifically, the Firm limited its procedures to comparing the current year's assumption to that used in the prior year noting consistency. The Firm, however, did not evaluate whether the assumption should have changed.
 - Performed procedures to evaluate whether data obtained from an external source that the Firm used to assess the reasonableness of the issuer's delinquency assumptions was derived from comparable loans.

A.7. Issuer G

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

- The Firm failed to identify and test any controls over gift card liabilities, and over rent expense and lease account balances and the related disclosures.

- The Firm's procedures to test certain review controls over sales and inventory were insufficient. Specifically, the Firm's procedures were limited to observing evidence that a review had occurred, and, for some controls, inquiring of management and/or comparing certain reports used in the control to other issuer documents, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements related to these areas. In addition, the Firm failed to test any controls over the accuracy and completeness of the data and reports used in the performance of certain of these review controls.
- The Firm failed to perform sufficient substantive procedures to test sales and inventory. The Firm designed its procedures based on a level of reliance on controls that was excessive due to the deficiencies in the Firm's testing of controls that are discussed above. As a result, the samples the Firm used to test sales and inventory were too small to obtain the necessary level of assurance. In addition, the Firm failed to test the accuracy and completeness of certain reports it used in its testing of sales.

A.8. Issuer H

In this audit, in addition to the deficiencies described in Part I.A.23 related to testing the fair value measurements of hard-to-value financial instruments, the Firm failed in the following respects to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and on the effectiveness of ICFR –

- The Firm failed to perform sufficient procedures to test certain review controls over the valuation of investments in securities, investments in real estate, and the ALL. Specifically, the Firm failed to assess whether the controls were designed to operate at a level of precision that would prevent or detect material misstatements.
- The Firm failed to perform sufficient substantive procedures to test the ALL. Specifically –
 - To evaluate the specific reserves, the Firm tested a sample of impaired loans that it selected by choosing every third loan on a list. The Firm's testing was insufficient, as the sampling resulted in the

Firm failing to test, beyond inquiry of management, any of the multiple impaired loans that had a net recorded value in excess of the Firm's established level of materiality.

- The Firm failed to perform sufficient procedures to test the specific reserves for certain of the impaired loans that it had selected for testing. Specifically, the Firm failed to evaluate the reasonableness of certain important assumptions, including the capitalization rates, and the cash flow projections that the issuer used in its determination of the value of the real estate that served as collateral for the loans. In addition, the Firm failed to test the mathematical accuracy of certain aspects of the specific-reserve calculations, including the cash flow projections.
- The Firm failed to perform sufficient procedures to test the issuer's loan risk-rating process, which the issuer used to identify impaired loans and evaluate whether the loans required a specific reserve. Specifically, there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had evaluated the qualitative factors, including current market conditions related to the underlying properties, that the issuer used to assign a risk rating to its loans. In addition, the Firm determined that certain loans, not on the issuer's watch list, that the Firm tested had an apparent shortfall between the operating cash flows for the real estate that served as collateral for the loan and the related debt service obligation; however, the Firm failed to evaluate the implications of these apparent shortfalls on the Firm's conclusions about the effectiveness of the issuer's loan risk-rating process.

A.9. Issuer I

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

- The Firm failed to sufficiently test certain review controls over revenue and the accounting for business combinations. Specifically, the Firm limited its procedures to inquiring of management, observing evidence that the

reviews had occurred, and/or tracing certain data used in the performance of the controls to source documents. There was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had evaluated whether the controls operated at a level of precision that would prevent or detect material misstatements.

- The Firm failed to perform sufficient substantive procedures to test the issuer's fixed-price revenue contracts with multiple deliverables, which consisted primarily of services. Specifically, the Firm failed to sufficiently evaluate the issuer's assessment of whether the multiple deliverables represented separate units of accounting. For certain contracts, the Firm concurred with the issuer's conclusion that the deliverables did not have value on a stand-alone basis because the issuer did not have a history of providing such deliverables separately; however, the Firm failed to consider whether (a) other vendors provided similar deliverables separately or (b) the customer could separately resell any of the non-service deliverables.

A.10. Issuer J

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

- The Firm's procedures to test review controls over the possible impairment of goodwill and other intangible assets, and over the valuation of the customer rebate reserve, were insufficient, as its testing of these controls was limited to inquiring of management or observing evidence of review and approval. In addition, the Firm stated that its substantive procedures provided evidence of the effectiveness of the control over the possible impairment of goodwill and other intangible assets. The Firm, however, failed to test, through any of its procedures, whether these controls operated at a level of precision that would prevent or detect material misstatements related to these areas.
- The Firm failed to sufficiently test controls over the accuracy and completeness of reports used in the operation of the issuer's review

control over the determination of inventory reserves. Specifically, the Firm relied on information technology general controls ("ITGCs") over the application that generated the reports. The Firm, however, identified an unremediated deficiency in change management controls over that application, and there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had performed procedures to evaluate the effect of that deficiency on its ability to rely on ITGCs.

- The Firm failed to perform sufficient substantive procedures to test the possible impairment of goodwill. The issuer calculated the fair value of its single reporting unit based on a weighted average of fair value estimates determined using three different valuation methods, one of which was the market capitalization method. The issuer assigned a ten percent weight to the market capitalization method and a 45 percent weight to the other two methods. The Firm failed to evaluate the reasonableness of the weighting that the issuer assigned to the values included in this calculation. In addition, the Firm failed to sufficiently evaluate the reasonableness of an assumption, which was used in two of the fair value estimates, regarding the fair value of synergies that would be realized by a likely buyer. Specifically, the Firm's procedures were limited to inquiring of management and comparing amounts included in the calculation to the issuer's accounting records. Further, the Firm failed to assess whether the fair value estimate determined by projecting cash flows was reasonable in light of the fact that the fair value estimates determined under the other two methods the issuer used were lower by a substantial amount, were lower than the recorded value of the reporting unit, and were similar to each other.
- The Firm failed to sufficiently evaluate the reasonableness of two important assumptions the issuer used to estimate the customer rebate reserve. Specifically, the Firm failed to test one of these assumptions, and it limited its testing of the second assumption to tracing certain data the issuer used to derive the assumption to customer reports that the issuer provided to the Firm.

A.11. Issuer K

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

- The Firm failed to sufficiently test review controls that it selected over the valuation of inventory, the possible impairment of goodwill and other indefinite-lived intangible assets, and the accounting for business combinations. Specifically, the Firm's procedures were limited to inquiring of management, reading memoranda used in certain of the controls, observing evidence that reviews had occurred, and/or verifying the mathematical accuracy of reports management used in the performance of these controls. In addition, the Firm referenced its substantive testing when addressing its evaluation of the effectiveness of certain of these controls. The Firm, however, failed to test, through any of its procedures, whether these controls operated at a level of precision that would prevent or detect material misstatements related to these areas.
- The issuer records a reserve for excess and obsolete inventory and makes other adjustments, when necessary, to reduce the value of inventory to the lower of cost or market. The Firm failed to perform sufficient substantive procedures to test the valuation of inventory, as follows –
 - For one business unit, the Firm assessed the inherent risk for the valuation of inventory as high, and the issuer recorded no excess and obsolete reserves for most of the inventory. The Firm's procedures to evaluate the reasonableness of this estimate, however, were limited to inquiring of management, noting that the majority of inventory items had a change in quantity during the year, and comparing various inventory ratios at the business unit level, such as inventory turnover rates and inventory reserves as a percentage of total inventory, to the same ratios for prior periods. In addition, the Firm failed to perform procedures to test whether inventory was recorded at the lower of cost or market.

- For a second business unit, the Firm limited its procedures to evaluate the reasonableness of the calculated inventory reserves to testing the mathematical accuracy of the calculation and considering inventory write-offs that occurred after the balance sheet date. In addition, the Firm failed to perform procedures to test whether inventory was recorded at the lower of cost or market.
- For a third business unit, the Firm's procedures to evaluate the reasonableness of the calculated inventory reserves consisted of testing reserves for product lines with inventory balances above an established threshold. This testing was deficient, as the Firm failed to –
 - Test the accuracy and completeness of certain data it used to test the reserves.
 - Sufficiently evaluate the reasonableness of the issuer not having recorded reserves for certain of the product lines, as the Firm's procedures were limited to observing that there was a certain minimal level of sales of those product lines subsequent to year end.
 - Perform any procedures to test the inventory reserves for the product lines with inventory balances below the established threshold; the inventory balances for these product lines were, in the aggregate, several times the Firm's established level of materiality.
 - Include sales incentives in its determination of the market value of inventory it selected for testing, when testing whether inventory was recorded at the lower of cost or market.

A.12. Issuer L

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

- The issuer's investment custodian initiated and processed investment transactions for the issuer, and the issuer used data from the custodian to record those transactions. The Firm failed to perform procedures to obtain evidence about the effectiveness of the controls over the accuracy of the data used to record those transactions.
- The Firm selected for testing two review controls over the accounting for business combinations, but it limited its procedures to inquiring of management, attending meetings that constituted part of the performance of the controls, and observing evidence of review. The Firm's procedures did not include testing whether the controls operated at a level of precision that would prevent or detect material misstatements.
- The Firm failed to sufficiently test the valuation of intangible assets acquired in a business combination. The issuer engaged an external specialist to determine the value of the intangible assets acquired, and provided revenue growth rate projections and historical data to the specialist for use in the valuation analysis. The Firm failed, beyond inquiry of management, to (a) evaluate the reasonableness of certain significant assumptions the issuer used to determine the projected revenue and (b) test the historical data.
- The Firm failed to identify and test any controls that addressed whether revenue from product sales was appropriately recognized upon shipment. In addition, the Firm selected for testing two manual controls related to the accuracy of sales and shipment data, but it failed to sufficiently test the operating effectiveness of these controls. Specifically, the manual controls operated multiple times each day, but the Firm limited its testing to only one transaction for each of these controls.
- The Firm failed to perform sufficient substantive procedures to test revenue from product sales, as it designed its procedures based on a level of reliance on controls that was excessive due to the deficiencies in the Firm's testing of controls that are discussed above. Specifically, the sample size the Firm used in its testing was insufficient to obtain the necessary level of assurance.

A.13. Issuer M

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

- The Firm selected for testing certain review controls over the issuer's accounting for business combinations, but its procedures to test those controls were not sufficient. Specifically, the Firm limited its procedures to observing evidence that a review had occurred and inquiring of management, without testing whether the controls operated at a level of precision that would prevent or detect material misstatements.
- The Firm's procedures to test certain revenue recorded using the percentage-of-completion method of accounting were insufficient. Specifically, the Firm selected certain contracts for testing, but it failed to evaluate, beyond inquiry of issuer personnel, the reasonableness of the estimated costs to complete the contracts, which the issuer used to calculate contract revenue.
- The Firm failed to perform sufficient procedures to test revenue from certain other contracts. The Firm's procedures to test these contracts were analytical procedures consisting of a comparison of gross margins between the third and fourth quarters of the year; however, due to deficiencies in these procedures, they provided little to no substantive assurance. Specifically, the Firm failed to establish a plausible relationship for the use of the third quarter gross margin data as a basis for its expectation, and it failed to test the accuracy of the data. In addition, the Firm failed to investigate certain differences that were above its established thresholds. For other such differences, it limited its procedures to inquiring of management, without obtaining corroboration of management's explanations.
- The issuer consummated two significant business combinations during the year and used external specialists to determine the fair value of assets acquired in those business combinations. The Firm failed to perform

sufficient procedures to test the valuation of certain of the acquired assets. Specifically –

- The Firm failed to sufficiently test the underlying cash flow projections the issuer provided to a specialist for use in valuing customer-relationship intangible assets. Specifically, the Firm limited its procedures to test the projected revenue to observing that a portion of the projected revenue appeared reasonable when compared to actual revenue in prior years. In addition, the Firm failed to perform any procedures to evaluate the reasonableness of the direct costs and selling, general, and administrative expenses included in the cash flow projections.
- The Firm failed to perform any procedures to test the significant adjustments made to the carrying value of the acquired inventory that the specialist used to determine the fair value of that inventory.
- The Firm failed to test the accuracy and completeness of data that the issuer provided to the specialists for use in determining the value of certain acquired assets.
- For one of the business combinations, there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had evaluated the reasonableness of certain assumptions the issuer's specialist used to estimate the fair value of certain property and equipment, beyond obtaining the specialist's valuation report and discussing the assumptions with the specialist.

A.14. Issuer N

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

- The Firm selected for testing a review control over the assessment of the possible impairment of certain long-lived assets. The Firm's procedures to test this control were limited to observing evidence that a review had

occurred, without evaluating whether the control operated at a level of precision that would prevent or detect material misstatements.

- The Firm's procedures to test the possible impairment of two significant properties held for development were insufficient.
 - For one of the properties, the issuer's external valuation specialist estimated the fair value as it was currently zoned, and as if zoning changes had occurred that would allow the issuer's planned use of that property. The Firm used the specialist's value determined as if the zoning changes had occurred to conclude that the property was not impaired, but failed to take into account information in the specialist's report that appeared inconsistent with the assumption that a change in the zoning for the property was likely to occur. In addition, the Firm failed to evaluate the reasonableness of the underlying assumptions the specialist used to determine the fair values.
 - The Firm failed to evaluate the reasonableness of environmental remediation cost estimates that the issuer provided to an external specialist for use in estimating the value of the second property.

A.15. Issuer O

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

- Within the issuer's largest segment, revenues are primarily generated by sales to wholesale customers ("commercial revenue") and retail sales ("retail revenue.") The Firm failed to identify and test any controls over the valuation of retail revenue.
- The Firm failed to perform sufficient procedures to test certain review controls that it selected over commercial revenue, and over retail accounts receivable and the related allowance for doubtful accounts. The Firm's testing of these controls was limited to obtaining evidence of review and

approval and, for certain controls, comparing data used in the operation of the control to supporting documentation, or verifying the mathematical accuracy of management's calculations. There was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had evaluated whether the controls operated at a level of precision that would prevent or detect material misstatements.

- The issuer accumulated in a database electronically generated data reflecting revenue transactions, and those data were transferred into the issuer's billing systems to calculate revenue. The Firm failed to test any controls over the accuracy and completeness of the data transferred into the commercial billing system.
- The Firm's substantive procedures to test the valuation of retail revenue were insufficient. Specifically, in the Firm's testing of a sample of transactions, it failed to test whether the rate used to calculate the revenue was appropriate.
- The Firm failed to perform sufficient substantive procedures to test the occurrence and completeness of commercial revenue. Specifically, the Firm's procedures were limited to testing two sales transactions, confirming accounts receivable at year end, and scanning the sales journal near year end for significant or unusual transactions.
- The Firm failed to perform sufficient procedures to test the existence of accounts receivable for the issuer's largest segment. The Firm's primary substantive test in this area was to confirm accounts receivable. The Firm selected customer accounts for testing that each exceeded a monetary threshold, but it limited its testing to only one invoice from each of those customer accounts. In addition, the Firm's other procedures to test the existence of the remaining accounts receivable balance did not reduce the risk related to that population to an appropriately low level, as the Firm's procedures consisted of testing only eight additional invoices (representing less than two percent of the remaining accounts receivable balance) through its performance of other substantive procedures, and these additional invoices were not selected in a manner designed to

produce a sample that was representative of the remaining accounts receivable.

A.16. Issuer P

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

- The Firm's testing of certain review controls over the valuation of inventory was insufficient, as its procedures were limited to inquiring of management and observing evidence that a review had occurred, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements.
- The Firm failed to sufficiently test controls over the completeness of the issuer's pension liability. Specifically, there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had performed procedures to obtain evidence about the effectiveness of any controls over certain data that constituted important inputs into the issuer's determination of its pension liability.

A.17. Issuer Q

In this audit, the Firm failed to perform sufficient procedures to test the ALL. The issuer used appraisals to determine the fair value of real estate that served as collateral for certain loans. There was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had evaluated the reasonableness of the assumptions that the appraisers used to value the underlying real estate, beyond reading the appraisal reports. In addition, the Firm failed to perform sufficient procedures to evaluate the competence and objectivity of the appraisers, as it limited its procedures to determining whether the appraisers were licensed and whether the appraisers were approved for use by the issuer's board of directors.

A.18. Issuer R

In this audit, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the effectiveness of ICFR. The Firm's procedures to test two

review controls, one over the selection of the revenue recognition method for sales contracts and one over the valuation of unbilled accounts receivable, were insufficient. Specifically, there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had performed procedures to test the effectiveness of these controls, beyond observing evidence of management's review and approval. In addition, the Firm stated that its substantive testing provided evidence of the effectiveness of one of these controls. The Firm, however, failed to test, through any of its procedures, whether the controls operated at a level of precision that would prevent or detect material misstatements related to these areas.

A.19. Issuer S

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

- The Firm's testing of certain review controls over the accounting for business combinations and the possible impairment of goodwill and other intangible assets was insufficient. Specifically, the Firm limited its procedures to inquiring of management or observing evidence of reviewer sign-off or approval and, for certain controls, comparing certain amounts to supporting documents or verifying the mathematical accuracy of calculations. In addition, the Firm stated that certain of its substantive procedures provided evidence of the effectiveness of these controls. The Firm, however, failed to test, through any of its procedures, whether the controls operated at a level of precision that would prevent or detect material misstatements related to these processes.
- Many of the issuer's business units had a significant amount of goodwill and other intangible assets, and the issuer had a history of recording impairment charges at the annual impairment assessment date and at interim dates. The Firm failed to identify and test any controls over the monitoring, between the issuer's annual impairment assessment dates, of indicators of possible impairment of goodwill and other intangible assets.

A.20. Issuer T

In this audit, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the effectiveness of ICFR. Specifically, the Firm selected for testing certain review controls over the assessment of the possible impairment of property and equipment, but it limited its procedures to testing the mathematical accuracy of the issuer's quarterly impairment analyses and inquiring of issuer personnel. The Firm's procedures did not include evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements related to the possible impairment of property and equipment.

A.21. Issuer U

In this audit, the Firm failed in the following respects to perform sufficient procedures to test revenue and deferred revenue –

- To test revenue and deferred revenue for one significant product line, the Firm used an attribute sampling approach and determined its sample size based on an expectation that there would be no testing exceptions within its sample. The issuer's revenue recognition policy provided that, for transactions with customer-acceptance terms, revenue would not be recognized until customer acceptance had been received. For two of the items within the Firm's sample, the issuer did not obtain customer acceptance, even though the invoices indicated that customer acceptance was required. There was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had performed procedures to support its conclusion that the recognition of revenue from these transactions was appropriate without the issuer having obtained customer acceptance. As a result, the Firm did not obtain sufficient evidence that there were no testing exceptions, which, given its testing strategy, was necessary to support its conclusion that revenue recognition for this product line was appropriate.
- The Firm failed to perform sufficient revenue cut-off testing, as it excluded certain types of invoices from the population from which it selected its sample for testing.

A.22. Issuer V

The majority of the issuer's revenue was calculated based on the number of electronically initiated transactions that occurred during the year. The Firm's procedures to test the accuracy and completeness of the transactional data used to calculate revenue were insufficient. Specifically, the Firm's approach for testing the applications generating and storing these data consisted of a "test of one;" this approach assumed effective ITGCs. The Firm failed to sufficiently test the operating effectiveness of ITGCs, however, as its tests of the majority of these controls were limited to inquiry of issuer personnel.

A.23. Deficiencies in Testing the Fair Value Measurements and Disclosures of Financial Instruments Without Readily Determinable Fair Values

In four audits,^{5/} due to deficiencies in testing related to hard-to-value financial instruments, including commercial mortgage-backed securities, collateralized mortgage and debt obligations, other real estate investments, and trust preferred securities, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements. The deficiencies are as follows –

- In each of these audits, the Firm failed to obtain an understanding of the specific methods and assumptions underlying fair value measurements that were obtained from pricing services or other external parties and used in the Firm's testing of certain hard-to-value financial instruments.
- In two of these audits,^{6/} the Firm tested the issuer's process for developing fair value measurements for certain hard-to-value financial instruments. The Firm, however, failed to evaluate the appropriateness of the valuation methods and the reasonableness of the important assumptions underlying the fair value measurements.

^{5/} Issuers D, E, F, and H

^{6/} Issuers D and F

- In two of these audits,^{7/} the Firm developed an independent estimate of fair value to test the fair value measurement of certain hard-to-value financial instruments. In one audit, the Firm used historical data to develop its assumptions,^{8/} and in the other audit, the Firm used historical knowledge about the issuer to develop expected price ranges.^{9/} In both audits, the Firm failed to evaluate whether the historical information reflected market conditions as of the valuation date and resulted in assumptions that were not inconsistent with assumptions market participants would use to value the financial instruments.

- In one of these audits,^{10/} to test the valuation of certain hard-to-value financial instruments, the Firm obtained estimates of fair value from two external parties. The Firm compared those values to the issuer's recorded values and established a threshold for investigating differences. The procedures the Firm performed were insufficient, as –
 - Many of the instruments had differences in excess of the Firm's established threshold; however, the Firm performed additional testing for only certain of these financial instruments.

 - When establishing thresholds for investigation of significant differences, the Firm failed to consider the possibility that a combination of differences could aggregate to an unacceptable amount. As a result, the Firm failed to investigate differences that, in combination, exceeded the Firm's established materiality level by a significant amount.

^{7/} Issuers F and H

^{8/} Issuer F

^{9/} Issuer H

^{10/} Issuer D

- In two of the audits,^{11/} the Firm failed to adequately test the issuers' disclosures of certain hard-to-value financial instruments as level 2 or level 3 because it failed to obtain an understanding of whether significant inputs used to value the financial instruments were observable or unobservable.

B. Auditing Standards

Each of the deficiencies described in Part I.A of this report represents circumstances in which the Firm failed to comply with the requirement to obtain sufficient appropriate evidence to support its opinion that the financial statements were presented fairly, in all material respects, in accordance with applicable accounting principles, and/or for its opinion concerning whether the issuer maintained, in all material respects, effective internal control over financial reporting. Each deficiency relates to several applicable standards that govern the conduct of audits.

AU 230, *Due Professional Care in the Performance of Work* ("AU 230") requires the independent auditor to plan and perform his or her work with due professional care. AU 230 and Auditing Standard ("AS") No. 13, *The Auditor's Responses to the Risks of Material Misstatement* ("AS No. 13") specify that due professional care includes the exercise of professional skepticism. This is an attitude that includes a questioning mind and a critical assessment of the appropriateness and sufficiency of audit evidence.

AS No. 13 requires the auditor to design and implement audit responses that address the identified risks of material misstatement, and AS No. 15, *Audit Evidence* ("AS No. 15") 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 and the quality of the audit evidence obtained. The appropriateness of evidence is measured by its quality; to be appropriate, evidence must be both relevant and reliable in support of the related conclusions.

AS No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* ("AS No. 5") and AS No. 13 establish requirements regarding testing and evaluating internal control over financial reporting. In an audit of internal control over financial reporting in an integrated audit, AS No. 5 requires the auditor to plan and perform the audit to obtain appropriate evidence that is

^{11/} Issuers E and H

sufficient to support the auditor's opinion on internal control over financial reporting as of the date of that opinion. AS No. 13 requires that, if the auditor plans to assess control risk at less than the maximum and to base the nature, timing, and extent of substantive audit procedures on that lower assessment, the auditor must obtain evidence that the controls tested were designed and operating effectively during the entire period for which the auditor plans to rely on controls to modify the substantive procedures.

The deficiencies described in Part I.A of this report relate to one or more of the provisions referenced above, and in many cases also relate to the failure to perform, or to perform sufficiently, certain specific audit procedures that are required by other applicable auditing standards. The table below lists the specific auditing standards that are primarily implicated by the deficiencies identified in Part I.A of this report. The broadly applicable aspects of AS No. 5, AS No. 13, AS No. 15, and AU 230 discussed above are not repeated in the table below.^{12/}

PCAOB Auditing Standards	Issuers
AS No. 5, <i>An Audit of Internal Control Over Financial Reporting That is Integrated with An Audit of Financial Statements</i>	A, B, C, D, E, F, G, H, I, J, K, L, M, N, O, P, R, S, and T
AS No. 13, <i>The Auditor's Responses to the Risks of Material Misstatement</i>	A, C, D, G, I, K, L, M, U, and V
AS No. 14, <i>Evaluating Audit Results</i>	A
AS No. 15, <i>Audit Evidence</i>	C, G, H, N, and V
AU 322, <i>The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements</i>	D and F
AU Section 326, <i>Evidential Matter</i>	B and O
AU Section 328, <i>Auditing Fair Value Measurements and Disclosures</i>	D, E, F, H, J, L, M, N, and Q
AU Section 329, <i>Substantive Analytical Procedures</i>	C and M
AU Section 332, <i>Auditing Derivative Instruments, Hedging Activities, and Investments in Securities</i>	A
AU Section 333, <i>Management Representations</i>	A
AU Section 336, <i>Using the Work of a Specialist</i>	L and Q
AU Section 342, <i>Auditing Accounting Estimates</i>	B, D, E, F, H, J, and K

^{12/} This table does not necessarily include reference to every auditing standard that may have been implicated by the deficiencies included in Part I.A.

PCAOB Auditing Standards	Issuers
AU Section 350, <i>Audit Sampling</i>	A, H, O, and U

C. General Information Concerning PCAOB Inspections

Board inspections are designed to identify whether weaknesses and deficiencies exist related to how a firm conducts audits and to address any such weaknesses and deficiencies. To achieve that goal, inspections include reviews of certain aspects of selected audit work performed by the Firm and reviews of certain aspects of the Firm's quality control system. The focus on weaknesses and deficiencies necessarily carries through to reports on inspections and, accordingly, Board inspection reports are not intended to serve as balanced report cards or overall rating tools. Further, the inclusion in an inspection report of certain deficiencies and potential deficiencies should not be construed as an indication that the Board has made any determination about other aspects of the firm's systems, policies, procedures, practices, or conduct not included within the report.

The inspection team selects the audits and aspects to review, and the Firm is not allowed an opportunity to limit or influence the selections. In the course of reviewing aspects of selected audits, the inspection team may identify matters that it considers to be deficiencies in the performance of the work it reviews. Those deficiencies may include failures by the Firm to identify, or to address appropriately, financial statement misstatements, including failures to comply with disclosure requirements,^{13/} as well as failures by the Firm to perform, or to perform sufficiently, certain necessary audit procedures. 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

^{13/} 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 applicable accounting principles, the Board's practice is to report that information to the Securities and Exchange Commission ("SEC" or "the Commission"), which has jurisdiction to determine proper accounting in issuers' financial statements. Any description in this report of financial statement misstatements or failures to comply with SEC disclosure requirements should not be understood as an indication that the SEC has considered or made any determination regarding these issues unless otherwise expressly stated.

Board inspection report should not be understood to provide any assurance that the firm's audit work, or the relevant issuers' financial statements or reporting on internal control, are free of any deficiencies not specifically described in an inspection report.

If the Board inspection team identifies deficiencies that exceed a certain significance threshold in the audit work it reviews, those deficiencies are summarized in the public portion of the Board's inspection report. The Board cautions, however, against extrapolating from the results presented in the public portion of the report to broader conclusions about the frequency of deficiencies throughout the Firm's practice. Audit work is selected for inspection largely on the basis of an analysis of factors that, in the inspection team's view, heighten the possibility that auditing deficiencies are present, rather than through a process intended to identify a representative sample.

In some cases, the conclusion 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 the firm claimed to have performed the procedure. AS 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.

Inclusion of a deficiency in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the firm's attention. When audit deficiencies are identified after the date of the audit report, PCAOB standards require a firm to take appropriate actions to assess the importance of the deficiencies to the firm's present ability to support its previously expressed audit opinions. Depending upon the circumstances, compliance with these 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 previously expressed audit opinions.^{14/}

^{14/} The inspection team may review, either in the same inspection or in subsequent inspections, the adequacy of the firm's compliance with these requirements. Failure by a firm to take appropriate actions, or a firm's misrepresentations in responding to an inspection report, about whether it has taken such actions, could be a basis for Board disciplinary sanctions.

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 processes related to audit quality. This review addressed practices, policies, and procedures concerning audit performance and the following five areas (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 clients, 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 audit clients; 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 weaknesses in quality control.

END OF PART I

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

APPENDIX C

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.^{1/}

^{1/} The Board does not make public any of a firm's comments that address a nonpublic portion of the report. In some cases, the result may be that none of a firm's response is made publicly available. In addition, pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(b), if a firm requests, and the Board grants, confidential treatment for any of the firm's comments on a draft report, the Board does not include those comments in the final report at all. The Board routinely grants confidential treatment, if requested, for any portion of a firm's response that addresses any point in the draft that the Board omits from, or any inaccurate statement in the draft that the Board corrects in, the final report.



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November 4, 2013

Re: Response to Part I of the Draft Report on the 2012 Inspection of Grant Thornton LLP

Dear Ms. Munter:

We appreciate the opportunity to respond to Part I of the Public Company Accounting Oversight Board's ("PCAOB") Draft Report on the 2012 Inspection of Grant Thornton LLP (the "Report"). We support the PCAOB's mission to protect the interests of investors and further the public interest in the preparation of informative, accurate and independent audit reports. We share these goals and recognize the important role the PCAOB's inspection process plays in improving audit quality, serving investors and safeguarding the public interest. The PCAOB inspection report and dialogue with the inspections staff is an integral component in focusing our efforts.

The volume of findings in this report is concerning and of great importance to our dedicated professionals. Nineteen of the 22 engagements included in Part 1 of this report (86%) include findings related to the audit of internal control over financial reporting (ICFR). These audits of 2011 financial statements were completed during or before the spring of 2012. In the summer of 2012 we revised our ICFR audit methodology and training in response to the PCAOB's increased concern about the quality of ICFR audits across the entire auditing profession. Those changes were in effect during our audits of 2012 financial statements and we believe have been effective at improving audit quality in this important area. At the same time we continue to strive for and are finding improved audit quality in other audit areas.

We carefully considered each of the report findings for the Issuer audits described in Part I of the Report. Accordingly, we took all steps necessary to fulfil our responsibilities under 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*.



We look forward to the continuing dialogue as we pursue our shared goals of improving audit quality across the profession and protecting the investing public.

Respectfully submitted,

By:

Handwritten signature of Stephen M. Chipman in cursive.

Stephen M. Chipman
CEO

Handwritten signature of R. Trent Gazzaway in cursive.

R. Trent Gazzaway
National Managing Partner of Audit Services