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**STAFF AUDIT PRACTICE ALERT NO. 14**

**IMPROPER ALTERATION OF AUDIT  
DOCUMENTATION**

**APRIL 21, 2016**

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Staff Audit Practice Alerts highlight new, emerging, or noteworthy circumstances that may affect how auditors conduct audits under, or otherwise comply with, the existing requirements of the standards and rules of the PCAOB and relevant laws. Auditors should determine the actions necessary to respond to these circumstances. The statements contained in Staff Audit Practice Alerts do not establish rules of the Board and do not reflect any Board determination or judgment about the conduct of any particular firm, auditor, or any other person.

The PCAOB staff has prepared this practice alert to emphasize that improperly altering audit documentation in connection with a PCAOB inspection or investigation violates PCAOB rules requiring cooperation with the Board's oversight activities and can result in disciplinary actions with severe consequences. Improperly altering audit documentation is also inconsistent with an auditor's professional duty to act with integrity and as a gatekeeper in the public securities markets. Evidence identified in connection with certain recent oversight activities has heightened the staff's concern about such misconduct.

Auditors should have a clear understanding of the requirements related to revising or supplementing documentation in compliance with PCAOB standards, which are described below. They should also understand that PCAOB staff is attentive to, and follows up on, indications of possible departures from those requirements, particularly in circumstances suggesting that auditors may have altered audit documentation in attempting to avoid detection of audit deficiencies by PCAOB inspections or enforcement staff. The consequences of providing improperly altered audit documentation to PCAOB inspectors or investigators may in many cases be far more severe than would be the consequences of the PCAOB staff identifying the audit deficiency that the revisions to the documentation attempt to obscure.

The staff has identified concerns in connection with recent inspections of a range of firms, including firms affiliated with global networks and other firms. For that reason, the staff also encourages the leadership of firms and the networks to reinforce the importance of compliance with the requirements described in this practice alert.

### **PCAOB Audit Documentation Requirements**

AS 1215 (currently Auditing Standard No. 3), *Audit Documentation*, establishes general requirements for documentation that auditors should prepare and retain in connection with engagements conducted pursuant to PCAOB standards.<sup>1</sup> Among other things, AS 1215 states that "[a]udit documentation should be prepared in sufficient detail to provide a clear understanding of its purpose, source, and the conclusions reached."<sup>2</sup> AS 1215 also provides that auditors "must have completed all necessary auditing procedures and obtained sufficient evidence to support the representations in the auditor's report" prior to the report release date.<sup>3</sup> Further, pursuant to AS 1215, "[a] complete and final set of audit documentation should be assembled for retention as of a date not more than 45 days after the report release date (*documentation completion date*)."<sup>4</sup>

PCAOB standards recognize that "[c]ircumstances may require additions to audit documentation after the report release date," and set forth requirements for making any such additions. Specifically, AS 1215 states:

Audit documentation must not be deleted or discarded after the documentation completion date, however, information may be added. Any documentation added must indicate the date the information was added, the name of the person who prepared the additional documentation, and the reason for adding it.<sup>5</sup>

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<sup>1</sup> These requirements apply to audits of issuers and audits and attestation engagements of brokers and dealers under Securities Exchange Act Rule 17a-5.

<sup>2</sup> AS 1215.04.

<sup>3</sup> AS 1215.15. The "report release date" is "the date the auditor grants permission to use the auditor's report in connection with the issuance of the company's financial statements." AS 1215.14.

<sup>4</sup> AS 1215.15.

<sup>5</sup> AS 1215.16.

Under PCAOB standards, audit documentation "is the written record of the basis for the auditor's conclusions."<sup>6</sup> It also "facilitates the planning, performance, and supervision of the engagement, and is the basis for the review of the quality of the work because it provides the reviewer with written documentation of the evidence supporting the auditor's significant conclusions."<sup>7</sup> Reviewers may include, among others, internal and external inspection teams.<sup>8</sup> The Board's adoption of the documentation requirements contained in AS 1215 reflected, in part, a determination "that a documentation standard that enables a PCAOB inspector to understand the work that was performed [by the auditor] is essential."<sup>9</sup>

### **Improper Alteration as a Violation of the Duty to Cooperate**

PCAOB Rule 4006, *Duty to Cooperate with Inspectors*, requires that "[e]very registered public accounting firm, and every associated person of a registered public accounting firm...cooperate with the Board in the performance of any Board inspection."<sup>10</sup> This duty to cooperate includes an obligation not to provide improperly altered documents or misleading information in connection with the Board's inspection processes.<sup>11</sup>

In the past several years, the Board has sanctioned firms and individuals for violating both their obligation to cooperate with Board inspections and AS 1215, as a result of those firms and individuals improperly deleting, adding, or altering documentation in connection with an inspection. The sanctions in those cases have

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<sup>6</sup> AS 1215.02.

<sup>7</sup> *Id.*

<sup>8</sup> See AS 1215.03.e.

<sup>9</sup> *Audit Documentation and Amendment to Interim Auditing Standards*, PCAOB Rel. No. 2004-006, at 5 (June 9, 2004).

<sup>10</sup> Pursuant to PCAOB Rule 4020T(c), *Interim Inspection Program Related to Audits of Brokers and Dealers*, Rule 4006 applies to inspections of audits of brokers and dealers, as well as to inspections of issuer audits.

<sup>11</sup> See *Nathan M. Suddeth, CPA*, PCAOB Rel. No. 105-2013-007 (Sept. 10, 2013) ¶ 4; *Dale Arnold Hotz, CPA*, PCAOB Rel. No. 105-2012-008 (Nov. 13, 2012) ¶ 7; *Peter C. O'Toole, CPA*, PCAOB Rel. No. 105-2011-005 (Aug. 1, 2011) ¶ 5; *Drakeford & Drakeford, LLC*, PCAOB Rel. No. 105-2009-002 (June 16, 2009) ¶ 8.

included revoking a firm's registration and barring individuals from being associated persons of registered firms.<sup>12</sup>

Recently, PCAOB enforcement staff has uncovered evidence of additional instances of similar misconduct, including evidence that registered firms and associated persons have improperly deleted, added to, or altered audit documentation in connection with Board inspections, and then presented the altered documents to PCAOB inspectors without informing the inspectors of the alterations. In certain instances, evidence indicates that documents were created shortly in advance of, or during, an inspection, backdated, and then made available to PCAOB inspectors without any disclosure of when they were actually created. These recent instances involve both domestic firms and non-U.S. firms, including members of global networks.

Improper alteration of audit documentation in connection with an inspection undermines the integrity of the Board's inspection processes and, as a result, impedes the Board's efforts to improve audit quality and fulfill its mission to protect investors and further the public interest in the preparation of informative, accurate, and independent audit reports. Changes and additions to audit documentation, if any, following the documentation completion date must be made strictly in accordance with AS 1215.<sup>13</sup> To reduce the risk of improper alteration of audit documentation in connection with a PCAOB inspection, it is important for registered firms to take actions to assure<sup>14</sup> that (1) work papers are properly archived; (2) work papers, once archived, are not improperly altered; and (3) the documentation provided to PCAOB inspectors for an audit is the originally-archived documentation for that audit (supplemented, as appropriate, in accordance with AS 1215).

The staff also reminds firms and individuals of the consequences of improperly altering audit documentation in connection with a PCAOB investigation. The Board may institute disciplinary proceedings and impose sanctions against firms and their associated persons for noncooperation with an investigation, including noncooperation involving improperly altering audit documentation.<sup>15</sup>

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<sup>12</sup> See cases cited in note 11, *supra*.

<sup>13</sup> See AS 1215.16.

<sup>14</sup> See, e.g., QC § 20.03, .17-.18, *System of Quality Control for a CPA Firm's Accounting and Auditing Practice*.

<sup>15</sup> See Section 105(b)(3) of the Sarbanes-Oxley Act of 2002, as amended, 15 U.S.C. § 7215(b)(3); PCAOB Rule 5110, *Noncooperation with an Investigation*; Rule 5300(b), *Sanctions*; see also *Henry Mendoza, CPA*, PCAOB Rel. No. 105-2014-004 (May 6, 2014) (barring auditor from being an associated person of a registered public

PCAOB staff gives higher priority to addressing conduct that threatens to undermine the integrity of the Board's regulatory oversight processes. Registered firms and associated persons should be aware that failures to cooperate with a Board inspection or investigation can result in a Board disciplinary action and the imposition of significant sanctions, including the revocation of a firm's PCAOB registration, a bar on an individual from further association with any registered firm, and civil money penalties.<sup>16</sup>

## Reporting Potential Violations, Including Self-Reporting

The staff urges registered firms or individuals that become aware of any improper alteration of audit documentation that has occurred in connection with a Board inspection or investigation to report that information to the Board. They can do so by directly contacting staff in the Division of Registration and Inspections or the Division of Enforcement and Investigations, or by contacting the PCAOB Tip and Referral Center, including anonymously.<sup>17</sup> In addition, in appropriate circumstances, individuals may make use of their firm's internal whistleblower and complaint systems to report improper alteration of audit documentation or other suspected misconduct. Registered firms and associated persons should also take note of the Board's policy regarding credit for extraordinary cooperation, through which the Board seeks, among other things, to incentivize firms and associated persons to voluntarily and timely self-report, correct, and remediate violative conduct.<sup>18</sup> Voluntary and timely self-reporting of violative conduct, including violations of the obligation to cooperate with Board inspections or investigations, may be a factor in determining whether to impose sanctions against a firm or person and what sanctions to impose.

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accounting firm for, among other things, improperly altering and making additions to audit documentation in connection with a PCAOB investigation).

<sup>16</sup> See cases cited in notes 11 and 15, *supra*. The Securities and Exchange Commission also has imposed significant sanctions on auditors who have improperly altered audit documentation in connection with a PCAOB inspection. See, e.g., *Timothy Quintanilla, CPA*, AAER-3748 (Feb. 25, 2016); *Peter Messineo, CPA*, AAER-3721 (Dec. 10, 2015).

<sup>17</sup> See [pcaobus.org/Enforcement/Tips/Pages/TipsForm.aspx](http://pcaobus.org/Enforcement/Tips/Pages/TipsForm.aspx). Auditors can also self-report any improper alteration of audit documentation to the Securities and Exchange Commission.

<sup>18</sup> See *Policy Statement Regarding Credit for Extraordinary Cooperation in Connection with Board Investigations*, PCAOB Rel. No. 2013-003 (Apr. 24, 2013) [pcaobus.org/Enforcement/Documents/Release\\_2013\\_003.pdf](http://pcaobus.org/Enforcement/Documents/Release_2013_003.pdf).

**Contact Information**

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