PCAOB
Public Company Accounting Oversight Board

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ORDER INSTITUTING DISCIPLINARY PROCEEDINGS, MAKING FINDINGS, AND IMPOSING SANCTIONS

In the Matter of Christopher E. Anderson, CPA,

Respondent.

PCAOB Release No. 105-2008-003

October 31, 2008

By this Order, the Public Company Accounting Oversight Board ("Board" or "PCAOB") is (1) suspending Christopher E. Anderson, CPA, from being associated with a registered public accounting firm for a period of one year from the date of this Order; (2) restricting him to the role of "assistant," as that term is used in the Board's interim auditing standards, AU § 311.02(a), for an additional period of one year following expiration of his suspension; and (3) imposing a civil money penalty in the amount of $25,000 against him. The Board is imposing these sanctions on the basis of its findings concerning Respondent's violations of PCAOB rules and auditing standards in auditing the 2003 financial statements of one issuer client.

I.

The Board deems it necessary and appropriate, for the protection of investors and to further the public interest in the preparation of informative, fair and independent audit reports, that disciplinary proceedings be, and hereby are, instituted pursuant to Section 105(c) of the Sarbanes-Oxley Act of 2002 ("Act") and PCAOB Rule 5200(a)(1) against Respondent.

II.

In anticipation of institution of these proceedings, and pursuant to PCAOB Rule 5205, Respondent has submitted an Offer of Settlement ("Offer") that the Board has determined to accept. Solely for purposes of this proceeding and any other proceedings brought by or on behalf of the Board, or to which the Board is a party, and without admitting or denying the findings herein, except as to the Board's jurisdiction over Respondent and the subject matter of these proceedings, which is admitted,

ORDER

Respondent consents to entry of this Order Instituting Disciplinary Proceedings, Making Findings, and Imposing Sanctions ("Order") as set forth below.

III.

On the basis of Respondent's Offer and information obtained by the Board in this matter, the Board finds[1/] that:

A. Respondent

1. Anderson, 46, of Lake Forest, Illinois, is a certified public accountant licensed in Illinois (license no. 065027203), Iowa (license no. R04739), Wisconsin (license no. 20478-1), Michigan (license no. 1101029802), and Washington (license no. 15285). At all relevant times, he was a partner in the Chicago, Illinois office of the registered public accounting firm of Deloitte & Touche, LLP ("Deloitte") and an associated person of a registered public accounting firm as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(i).

B. Summary

2. This matter concerns Respondent's violations of PCAOB rules and auditing standards in auditing the fiscal year ("FY") 2003 financial statements of Navistar Financial Corporation ("NFC"). Respondent's failures occurred in the context of NFC's discovery – shortly before NFC and its parent, Navistar International Corporation ("NIC"), planned to file their Forms 10-K – of approximately $19.7 million in

[1/] The findings herein are made pursuant to Respondent's Offer and are not binding on any other person or entity in this or any other proceeding. The sanctions that the Board is imposing in this Order may be imposed only if a respondent's conduct meets one of the conditions set out in Section 105(c)(5) of the Act, 15 U.S.C. § 7215(c)(5). The Board finds that Respondent's conduct described in this Order meets the condition set out in Section 105 (c)(5), which provides that such sanctions may be imposed in the event of: (A) intentional or knowing conduct, including reckless conduct, that results in violation of the applicable statutory, regulatory, or professional standard; or (B) repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standard.

PCAOB
Public Company Accounting Oversight Board

ORDER

apparent errors resulting in an overstatement of NFC's assets, revenues, and earnings (the "overstatement"). Upon discovery of the overstatement, NIC faced the prospect of having to report fourth-quarter earnings below those announced to analysts and investors two weeks before.

3. Faced with management's interest in avoiding a retraction of that announcement and in meeting the companies' internal target date for filing their Forms 10-K, Respondent violated PCAOB standards in auditing NFC's FY 2003 financial statements and authorizing an unqualified audit opinion. After discovery of the overstatement, Respondent (1) accepted a decision, made at Deloitte's NIC engagement team level, that the quantitative materiality threshold for the NFC audit should be increased by 50 percent, even though Respondent believed that the original threshold remained appropriate and understood that the increased threshold would make it easier to treat known misstatements as immaterial; (2) accepted, without a reasonable basis, NFC accounting decisions and adjustments that offset the effect of the overstatement; (3) authorized issuance of the audit opinion before NFC completed reconciliation of the accounts that were the source of the overstatement; and (4) otherwise failed to act with the requisite due professional care and professional skepticism.

C. Respondent Failed to Comply with PCAOB Auditing Standards in Auditing the Financial Statements of Navistar Financial Corporation for FY 2003

4. NFC is a Delaware corporation with principal executive offices in Rolling Meadows, Illinois. NFC issues debt securities in the public markets and is required to file reports under Section 15(d) of the Securities Exchange Act of 1934. At all relevant times, NFC was an "issuer" as that term is defined by Section 2(a)(7) of the Act and PCAOB Rule 1001(i)(iii). At all times relevant to this Order, NFC, a second-tier, wholly-owned subsidiary of NIC,[2/] provided financing for new and used trucks sold by another NIC subsidiary and its dealers. NFC's results are consolidated into NIC's financial statements. At the time of the events described in this Order, Deloitte (and its

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[2/] NIC's common stock is registered under Section 12(b) of the Securities Exchange Act of 1934 and, at all times relevant to this Order, was listed on the New York Stock Exchange. NIC is an "issuer" as that term is defined in the Act and Board rules.

predecessors) had served as the outside auditor for NIC (and its predecessors) for nearly a century.

5. Respondent was the engagement partner for each of Deloitte's audits and reviews of NFC's financial statements from the beginning of FY 2000 through the end of FY 2003. In an audit report dated December 18, 2003, and included in NFC's Form 10-K filed with the Securities and Exchange Commission (the "Commission") on December 19, 2003, Deloitte expressed an unqualified opinion on NFC's statements of consolidated financial condition as of October 31, 2003 and October 31, 2002, and the related statements of consolidated income and cash flow for each of the three years in the period ended October 31, 2003. Deloitte's audit report stated that, in Deloitte's opinion, the audit had been conducted in accordance with U.S. generally accepted auditing standards[3/] and that NFC's financial statements presented fairly, in all material respects, its financial position in conformity with U.S. generally accepted accounting principles ("GAAP"). Respondent had final responsibility for the NFC audit as that phrase is used in AU § 311, *Planning and Supervision*, and authorized issuance of the audit report on December 18, 2003, concurrent with Deloitte's issuance of the NIC FY 2003 audit report.

6. In connection with the preparation or issuance of an audit report, PCAOB rules require that associated persons of registered public accounting firms comply with the Board's auditing standards.[4/] Under these standards, an auditor may express an

[3/] Deloitte's audit report for NFC stated that its audit was conducted in accordance with generally accepted auditing standards in the United States of America ("GAAS"). Respondent was required to conduct the audit in accordance with the PCAOB's interim auditing standards pursuant to PCAOB Rule 3200T, which took effect on April 25, 2003. However, at the time of the FY 2003 NFC audit, the PCAOB's interim auditing standards were the same as GAAS as it existed on April 16, 2003, and, until PCAOB Auditing Standard No. 1 took effect on May 24, 2004, it remained appropriate for auditors to refer to GAAS in their audit reports. Accordingly, although the reference to GAAS in Deloitte's report for NFC was appropriate at the time, the standards pursuant to which the audit was required to be performed are more appropriately referred to as PCAOB auditing standards (or PCAOB standards), and that is how they are referred to in this Order.

[4/] See PCAOB Rules 3100, 3200T.

Public Company Accounting Oversight Board

ORDER

unqualified opinion on an issuer's financial statements only when the auditor has formed such an opinion on the basis of an audit performed in accordance with PCAOB standards.[5/] Among other things, those standards require that an auditor exercise due professional care, exercise professional skepticism, and obtain sufficient competent evidential matter to afford a reasonable basis for an opinion regarding the financial statements.[6/] Under PCAOB standards, representations from management are part of the evidential matter that an auditor obtains, but management representations are not a substitute for the application of those auditing procedures necessary to afford a reasonable basis for the auditor's opinion.[7/] PCAOB standards also provide that when information comes to an auditor's attention that differs significantly from the information on which the audit plan was based, the auditor may need to re-evaluate his or her audit procedures based on a revised consideration of audit risk and materiality.[8/] Respondent failed to comply with these standards in connection with NFC's FY 2003 audit.

Background

7. NFC disclosed that its business included securitizing and selling loans and leases through special purpose entities, which then issued securities to investors. NFC retained interests in, and continued to service, the securitized loans and leases. After the FY 2002 audit of NFC's financial statements, Deloitte issued a management letter which, among other things, noted significant unreconciled items in suspense accounts that NFC used to account for cash disbursements and collections related to the securitization transactions. The management letter recommended improvements to the reconciliation process and, in FY 2003, Deloitte's NFC engagement team ("the engagement team") informed NFC that NFC needed to complete the suspense account reconciliations before the end of the FY 2003 audit and issuance of the NFC audit report. In addition, by FY 2003, the engagement team had identified what it believed to

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5/ See AU § 508.07, *Reports on Audited Financial Statements*.

6/ See AU § 150.02, *Generally Accepted Auditing Standards*; AU § 230, *Due Professional Care in the Performance of Work*; AU § 326, *Evidential Matter*.

7/ See AU § 333, *Management Representations*.

8/ See AU § 312, *Audit Risk and Materiality in Conducting an Audit*.

PCAOB
Public Company Accounting Oversight Board

ORDER

be certain deficiencies in NFC's methodology for calculating gains on the securitization transactions.

8. In FY 2003, NFC sold a total of $1.705 billion of loans and leases in three separate securitization transactions. For both the "2002-B" transaction in the first quarter and the "2003-A" transaction in the third quarter, NFC calculated the gains using the same methodology and estimates it had previously been using. For the "2003-B" transaction, in the fourth quarter, NFC calculated the gains using a new methodology (devised in consultation with the engagement team) and certain new estimates. NFC also re-ran the gain calculation for the 2003-A securitization using its new methodology. The engagement team compared the results of that recalculation to the results NFC previously had reached and recorded using its old methodology. The engagement team found no material difference in the results and, as late as December 14, 2003, concluded that the estimates used in all the gain calculations for FY 2003 "appear reasonable in all material respects."

Earnings Announcement and Subsequent Discovery of Overstated Balances

9. On December 2, 2003, NIC management hosted a conference call with securities analysts to announce, among other things, NIC's fourth-quarter and year-end results. NIC informed analysts that its fourth-quarter net income from continuing operations, when adjusted for restructuring costs, was $0.72 per share. NIC management specifically noted that these results were "on the top side of the previous guidance we had provided" to the public at the end of the third quarter.[9/] Before the December 2 call, Deloitte had informed NIC that the FY 2003 audits of NIC and NFC were substantially completed and that unqualified opinions were expected to be issued.

10. By no later than December 8, 2003, Respondent expected that Deloitte's audit reports for NIC and NFC would be issued and NIC's and NFC's Forms 10-K would be filed with the Commission on or about December 19, 2003. This expectation was consistent with NIC's and NFC's goal, and past practice, of filing their Forms 10-K with the Commission before the Christmas holiday, several weeks in advance of the regulatory filing deadline (which in this case was January 29, 2004).

[9/] In August 2003, NIC management had informed analysts that "[w]e anticipate we will be solidly profitable in the fourth quarter with diluted earnings of between $0.65 and $0.75 per share from continuing operations."

PCAOB
Public Company Accounting Oversight Board

ORDER

11. As of December 16, 2003, the engagement team was still awaiting NFC's suspense account reconciliations that had been noted in Deloitte's FY 2002 management letter. On the evening of December 16, 2003, Respondent was advised, as a result of the ongoing suspense account reconciliations, that the balances of certain NFC accounts were overstated. Specifically, Respondent was advised that cash outlays totaling approximately $17.7 million had not been appropriately recorded, and that an asset, now worthless, was recorded on NFC's books at approximately $2.0 million. Respondent concluded that these errors, totaling approximately $19.7 million, resulted in an overstatement of NFC's assets, revenue, and earnings.

NFC's Adjustments to Address the Overstatement

12. Because NFC's results are consolidated into NIC's financial statements, a write-off of the overstatement would reduce NIC's fourth-quarter earnings below what NIC had previously announced. Faced with that prospect, NFC, over December 17 and 18, made a series of accounting decisions that had the net result of avoiding any impact on NIC's reported earnings. First, NFC identified rationales for writing off less than half of the $19.7 million in 2003. Second, through recalculations of estimated gains, NFC recorded purported additional gains that offset those write-offs.

NFC's Decision to Write Off Only $7.294 Million in 2003

13. The overstatement of account balances had two basic components. One component was a $2,041,814 "hanging debit," which represented a recorded asset related to a FY 1999 securitization transaction (the 1999-B securitization). The debit was remaining (or "hanging") on NFC's balance sheet after the 1999-B securitization was settled in FY 2003. Because the securitization would not generate any future cash flows, the recorded asset was worthless. NFC wrote off this $2,041,814.

14. The remaining component—amounting to $17,645,115—involved what NFC had identified during the reconciliation process as incorrect accounting entries for cash outlays related to three securitization transactions (the 2000-C, 2001-B and 2002-B transactions). Respondent concluded that this component of the overstatement inflated the value of both an asset and a revenue account related to NFC's retained interests in the securitizations. Of the $17,645,115 component of the overstatement, NFC decided not to write off $7,768,145 related to the 2001-B and 2002-B transactions. The engagement team's work papers reflected that NFC's rationale for that decision was an analysis purportedly showing that the fair values of NFC's retained interests in

PCAOB
Public Company Accounting Oversight Board

ORDER

the 2001-B and 2002-B transactions exceeded their book values, even when all cash outlays were considered, thus purportedly rendering unnecessary any adjustment to the accounts related to those retained interests.

15. Of the $9,876,970 that related to the 2000-C transaction, the audit work papers reflected that, on the basis of the same type of analysis described above, NFC determined that $215,129 did not need to be written off. Of the remaining $9,661,841, NFC decided to write off only $5,173,512 in FY 2003, and indicated to Respondent that it would write off the remaining $4,488,329 in FY 2004.

16. In sum, of the $19.7 million in overstated account balances, NFC wrote off only $7,215,326 in FY 2003: the $2,041,814 hanging debit and $5,173,512 relating to the 2000-C transaction. At the same time, NFC made a separate, unexplained adjustment writing off an additional $78,674, bringing the total write-offs in FY 2003 to $7,294,000.

<u>NFC's Adjustments that Offset $7.294 Million in Write-Offs</u>

17. After identifying the overstatement, NFC recalculated the gains it previously had reported on sales related to the first two securitization transactions for FY 2003 – the 2002-B and 2003-A transactions. Whereas NFC had used its old methodology and estimates in initially calculating and reporting gains on those sales, NFC applied its new methodology and estimates in performing the recalculations. As a result, NFC arrived at an additional $6.259 million in gains.

18. NFC also made certain changes to the gain it initially calculated on sales related to the 2003-B transaction. Specifically, NFC reallocated certain transaction expenses between FY 2003 and FY 2004 and made certain interest rate adjustments. These changes resulted in additional gains of $1.035 million for FY 2003. Adding this $1.035 million to the $6.259 million derived from recalculating the 2002-B and 2003-A gains resulted in $7.294 million in additional gains.

19. Accordingly, in financial statements filed with NFC's Form 10-K on December 19, 2003 – three days after the $19.7 million overstatement was identified – the effect of the overstatement, including any potential impact on NIC's reported earnings, was neutralized by the decisions and adjustments described above. NFC's Form 10-K filing was accompanied by a Deloitte audit report, which Respondent authorized to be released on December 18, expressing an unqualified opinion on NFC's financial statements.

PCAOB
Public Company Accounting Oversight Board

ORDER

Respondent's Auditing Failures

20. Under the circumstances described above, an auditor proceeding in compliance with PCAOB standards would recognize the need to consider whether NFC's last-minute adjustments called for the auditor to revise his assessment of the risk of material misstatement due to fraud,[10/] or otherwise to reconsider the nature, timing, or extent of audit procedures[11/] in order to obtain the appropriate level of assurance concerning the financial statements. More generally, the due professional care required by PCAOB standards includes the element of professional skepticism, which is "an attitude that includes a questioning mind and a critical assessment of audit evidence" and an unwillingness to "be satisfied with less than persuasive evidence."[12/]

10/ PCAOB standards require an auditor, without making assumptions about whether management is honest or dishonest (see AU § 230.09), to respond to certain events – including "last-minute adjustments by the entity that significantly affect financial results" and "undue time pressures imposed by management to resolve complex or contentious issues" – by factoring them into an objective assessment of the risk of material misstatement due to fraud. See AU § 316.68, *Consideration of Fraud in a Financial Statement Audit*. (In the predecessor version of AU § 316, which was in effect for the audit of NFC's FY 2003 financial statements, the corresponding provision is found at ¶ 25, rather than ¶ 68. See AU § 316A.25.)

11/ Faced with factors suggesting an increased risk of material misstatement due to fraud, the application of appropriate professional skepticism involves such things as considering the need for additional procedures and additional corroboration of management's explanations or representations. See AU § 316.46. (In the predecessor version of AU 316, which was in effect for the audit of NFC's FY 2003 financial statements, the corresponding provision is found at ¶ 27, rather than ¶ 46. See AU § 316A.27.) Even apart from any risk of misstatement due to fraud, when information comes to an auditor's attention that differs significantly from the information on which the audit plan was based, the auditor may need to re-evaluate his or her audit procedures based on a revised consideration of audit risk and materiality. See AU § 312.33, *Audit Risk and Materiality in Conducting an Audit*.

12/ See AU §§ 230.07, 230.09.

PCAOB
Public Company Accounting Oversight Board

ORDER

21. Following the December 16 discovery of the overstatement, however, Respondent did not comply with these standards. On each of the points described below, Respondent accepted, without reasonable basis, NFC's rationales for concluding that the overstatement did not affect earnings and, thus, failed to obtain sufficient competent evidential matter to support the unqualified opinion on NFC's financial statements.

22. In planning the audit, Respondent had set, at $4.1 million, the quantitative threshold used by the engagement team to, among other things, determine whether to treat a misstatement in NFC's financial statements as presumptively material. But shortly after the overstatement was discovered, he accepted a decision, made at Deloitte's NIC engagement team level, that the threshold for the NFC audit should be increased to $6.1 million. Respondent accepted that decision even though he had final responsibility for the NFC audit, believed that the original materiality threshold remained appropriate, and understood that the increased threshold would make it easier to treat known misstatements as immaterial.

23. The increased materiality threshold affected the engagement team's assessment of the approximately $4.5 million component of the overstatement related to the 2000-C transaction. Respondent understood that NFC intended to postpone the write-off of the $4.5 million to FY 2004, rather than take the write-off in FY 2003. He identified NFC's failure to write off the $4.5 million in FY 2003 as resulting in a misstatement. Had he applied the original $4.1 million materiality threshold, he would have been required by Deloitte internal guidance to treat that unadjusted audit difference as a presumptively material departure from GAAP.[13/] Applying the 50 percent higher threshold, however, Respondent treated the $4.5 million as presumptively immaterial on a quantitative basis. As a result, Respondent failed to evaluate with due care and professional skepticism whether the $4.5 million unadjusted audit difference was in fact material to NFC's financial statements.

[13/] Deloitte's internal guidance concerning evaluation of misstatements provided, in part: "If known misstatements (net of tax effects, if applicable), either individually or in the aggregate, exceed planning materiality, we generally conclude that the financial statements are materially misstated. In such event, the client needs to adjust some or all of the known misstatements until we can conclude that aggregate unadjusted misstatements are acceptably small."

PCAOB
Public Company Accounting Oversight Board

ORDER

24. Respondent also failed to evaluate with due care and professional skepticism NFC's approach to the approximately $7.8 million in errors related to the 2001-B and 2002-B transactions. Specifically, Respondent failed to evaluate whether, consistent with GAAP, NFC could avoid writing off the overstatement to income by identifying a purported unrealized gain on the fair value of a related asset.

25. Further, Respondent did not adequately assess the appropriateness of NFC's recalculation of gains on sales related to the three securitization transactions in 2003. Although Respondent knew that the recalculations resulted in $7.294 million of additional gains – which offset the portion of the overstatement that NFC had determined to write off – he did not evaluate with due care and professional skepticism whether that result might have been achieved by making inappropriate changes to previously reported estimates, including estimates that he knew had previously been judged by the engagement team to appear reasonable in all material respects. Moreover, even aside from that failure, Respondent noted that the recalculated gains were overstated by $1.5 million because of NFC's rounding of certain items to the nearest million, a practice which he specifically advised NFC to discontinue for future periods.[14/] Respondent neither caused NFC to reduce the additional recorded gains nor included the $1.5 million overstatement on the schedule of unadjusted audit differences.

26. Finally, even though he knew that the reconciliation process had already uncovered the approximately $19.7 million overstatement, Respondent authorized release of an unqualified audit opinion for FY 2003 before NFC had completed the suspense account reconciliations.[15/]

[14/] The new gain calculations also included several mathematical and input errors, all of which increased the recalculated gains, and none of which Respondent detected.

[15/] After the audit report was released and NFC's Form 10-K for FY 2003 was filed, the ongoing reconciliation process revealed that certain amounts partially written off in connection with the 2000-C securitization had not been recorded in error and need not have been written off.

PCAOB
Public Company Accounting Oversight Board

ORDER

IV.

In view of the foregoing, and to protect the interests of investors and further the public interest in the preparation of informative, fair, and independent audit reports, the Board determines it appropriate to impose the sanction agreed to in Respondent's Offer. Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 105(c)(4)(B) of the Act and PCAOB Rule 5300(a)(2), Christopher E. Anderson is suspended for one (1) year from the date of this Order from being an associated person of a registered public accounting firm, as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(1);

B. Pursuant to Section 105(c)(4)(C) of the Act and PCAOB Rule 5300(a)(3), for one (1) year following the termination of the suspension ordered in paragraph A, Christopher E. Anderson's role in any audit of the financial statements of an issuer shall be restricted to that of "assistant," as that term is used in the Board's interim auditing standards, AU § 311.02(a), and may not include serving as the auditor with final responsibility for the audit (or any functionally equivalent but differently denominated role, such as "lead engagement partner" or "practitioner-in-charge") and may not include exercising authority either to sign a registered public accounting firm's name to an audit report or to consent to the use of a previously issued audit report for any issuer;

C. Pursuant to Section 105(c)(4)(D) of the Act and PCAOB Rule 5300(a)(4), a civil money penalty in the amount of $25,000 is imposed. All funds collected by the Board as a result of the assessment of this civil money penalty will be used in accordance with Section 109(c)(2) of the Act. Anderson shall pay this civil money penalty within 10 days of the issuance of this Order by (a) United States postal money order, certified check, bank cashier's check or bank money order; (b) made payable to the Public Company Accounting Oversight Board; (c) delivered to the Controller, Public Company Accounting Oversight Board, 1666 K Street, N.W., Washington, D.C. 20006; and (d) submitted under a cover letter which identifies Christopher E. Anderson as a respondent in these proceedings, sets forth the title and PCAOB Release number of these proceedings, and states that payment is made pursuant to this Order, a copy of which cover

Public Company Accounting Oversight Board

ORDER

letter and money order or check shall be sent to Office of the Secretary, Attention: J. Gordon Seymour, General Counsel and Secretary, Public Company Accounting Oversight Board, 1666 K Street, N.W., Washington, D.C. 20006.

ISSUED BY THE BOARD.

/s/ J. Gordon Seymour

J. Gordon Seymour
Secretary

October 31, 2008