2023 Inspection

BDO USA, P.C.

(Headquartered in Chicago, Illinois)

May 23, 2024

PCAOB

PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

PCAOB RELEASE NO. 104-2024-075

EXECUTIVE SUMMARY

Our 2023 inspection report on BDO USA, P.C. provides information on our inspection to assess the firm's compliance with Public Company Accounting Oversight Board (PCAOB) standards and rules and other applicable regulatory and professional requirements. This executive summary offers a high-level overview of what is included in this report:

- Part I.A of the report discusses deficiencies ("Part I.A deficiencies") in certain issuer audits that were of such significance that we believe the firm, at the time it issued its audit report(s), had not obtained sufficient appropriate audit evidence to support its opinion(s) on the issuer's financial statements and/or internal control over financial reporting (ICFR).

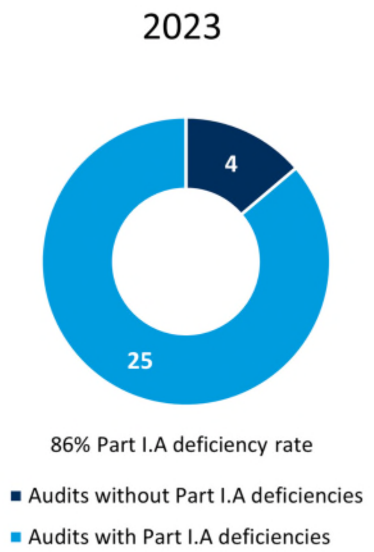
- Part I.B of the report discusses certain deficiencies ("Part I.B deficiencies") that relate to instances of non-compliance with PCAOB standards or rules other than those where the firm had not obtained sufficient appropriate audit evidence to support its opinion(s). This section does not discuss instances of potential non-compliance with SEC rules or instances of non-compliance with PCAOB rules related to maintaining independence.

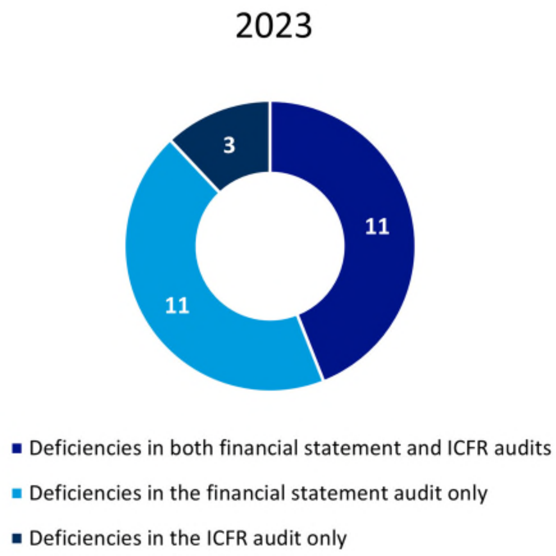
- Part I.C of the report discusses instances of potential non-compliance with SEC rules or instances of non-compliance with PCAOB rules related to maintaining independence ("Part I.C deficiencies").

If we include a Part I.A or Part I.B deficiency in this report — other than those deficiencies for audits with incorrect opinions on the financial statements and/or ICFR — it does not necessarily mean that the issuer's financial statements are materially misstated or that undisclosed material weaknesses in ICFR exist. If we include a Part I.C deficiency in this report, it does not necessarily mean that the Board has concluded the firm was not objective and impartial throughout the audit and professional engagement period. If we include a deficiency in Part I.A, Part I.B, or Part I.C of this report, it does not necessarily mean that the firm has not addressed the deficiency.

Overview of the 2023 Deficiencies Included in Part I

Twenty-five of the 29 audits we reviewed in 2023 are included in Part I.A of this report due to the significance of the deficiencies identified. The identified deficiencies primarily related to the firm's testing of controls over and/or substantive testing of revenue and related accounts, inventory, and business combinations.





In connection with our 2023 inspection procedures for one audit, the issuer restated its financial statements to correct misstatements, and the firm revised and reissued its report on the financial statements. In addition, in connection with our 2023 inspection procedures for another audit, the issuer revised its report on ICFR, and the firm revised its opinion on the effectiveness of the issuer's ICFR to express an adverse opinion and reissued its report.

The most common Part I.A deficiencies in 2023 related to identifying controls related to a significant account or relevant assertion, performing substantive testing to address a risk of material misstatement, and testing the design or operating effectiveness of controls selected for testing.

The Part I.B deficiencies in 2023 related to consideration of fraud, retention of audit documentation, audit committee communications, risk assessment, the firm's audit report, management communications, critical audit matters, and Form AP.

The Part I.C deficiencies in 2023 related to audit committee pre-approval and an indemnification clause.

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2023 INSPECTION

In the 2023 inspection of BDO USA, P.C., the PCAOB assessed the firm's compliance with laws, rules, and professional standards applicable to the audits of public companies.

We selected for review 29 audits of issuers with fiscal years generally ending in 2022. For each issuer audit selected, we reviewed a portion of the audit. We also evaluated elements of the firm's system of quality control.

What's Included in this Inspection Report

This report includes the following sections:

- **Overview of the 2023 Inspection and Historical Data by Inspection Year:** Information on our inspection, historical data, and common deficiencies.

- **Part I – Inspection Observations:**

    - **Part I.A:** Deficiencies that were of such significance that we believe the firm, at the time it issued its audit report(s), had not obtained sufficient appropriate audit evidence to support its opinion(s) on the issuer's financial statements and/or ICFR.

    - **Part I.B:** Certain deficiencies that relate to instances of non-compliance with PCAOB standards or rules other than those where the firm had not obtained sufficient appropriate audit evidence to support its opinion(s). This section does not discuss instances of potential non-compliance with SEC rules or instances of non-compliance with PCAOB rules related to maintaining independence.

    - **Part I.C:** Instances of potential non-compliance with SEC rules or instances of non-compliance with PCAOB rules related to maintaining independence.

  Consistent with the Sarbanes-Oxley Act ("Act"), it is the Board's assessment that nothing in Part I of this report deals with a criticism of, or potential defect in, the firm's quality control system. We discuss any such criticisms or potential defects in Part II. Further, you should not infer from any Part I deficiency, or combination of deficiencies, that we identified a quality control finding in Part II.

- **Part II – Observations Related to Quality Control:** Criticisms of, or potential defects in, the firm's system of quality control. Section 104(g)(2) of the Act restricts us from publicly disclosing Part II deficiencies unless the firm does not address the criticisms or potential defects to the Board's satisfaction no later than 12 months after the issuance of this report.

- **Appendix A – Firm's Response to the Draft Inspection Report:** The firm's response to a draft of this report, excluding any portion granted confidential treatment.

2023 Inspection Approach

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

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

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

Our target team performs inspection procedures in areas of current audit risk and emerging topics and focuses its reviews primarily on evaluating the firm's procedures related to that risk or topic. In 2023, our target team focused on the planning and execution of a multi-location audit.

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

OVERVIEW OF THE 2023 INSPECTION AND HISTORICAL DATA BY INSPECTION YEAR

The following information provides an overview of our 2023 inspection as well as data from the previous two inspections. We use a combination of risk-based and random methods to select audits for review and to identify areas on which we focus our review. Because our inspection process evolves over time, it can, and often does, focus on a different mix of audits and audit areas from year to year and firm to firm. As a result of this variation, we caution that our inspection results are not necessarily comparable over time or among firms.

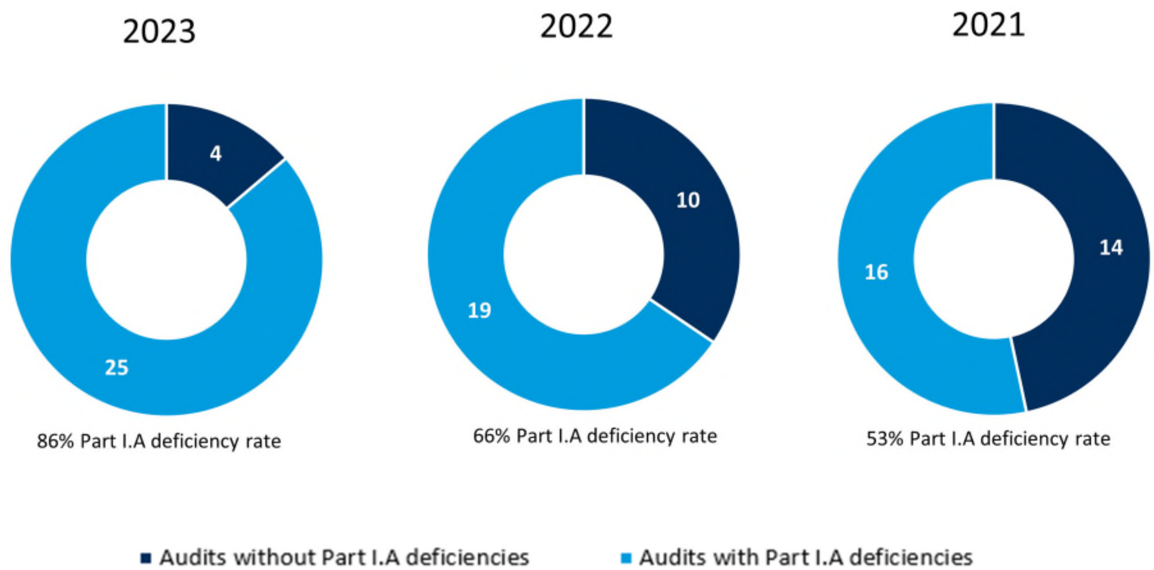
Audits Selected for Review

	2023	2022	2021
Total audits reviewed			
Total audits reviewed	29	29	30
Selection method			
Risk-based selections	22	20	14
Random selections	6	7	11
Target team selections[1]	1	2	5
Total audits reviewed	**29**	**29**	**30**
Principal auditor			
Audits in which the firm was the principal auditor	29	29	30
Audits in which the firm was not the principal auditor	0	0	0
Total audits reviewed	**29**	**29**	**30**
Audit type			
Integrated audits of financial statements and ICFR	19	19	15
Financial statement audits only	10	10	15
Total audits reviewed	**29**	**29**	**30**

[1] For further information on the target team's activities in 2022 and 2021, refer to those inspection reports.

Part I.A Deficiencies in Audits Reviewed

In 2023, 19 of the 25 audits appearing in Part I.A were selected for review using risk-based criteria. In 2022, 14 of the 19 audits appearing in Part I.A were selected for review using risk-based criteria. In 2021, 10 of the 16 audits appearing in Part I.A were selected for review using risk-based criteria.

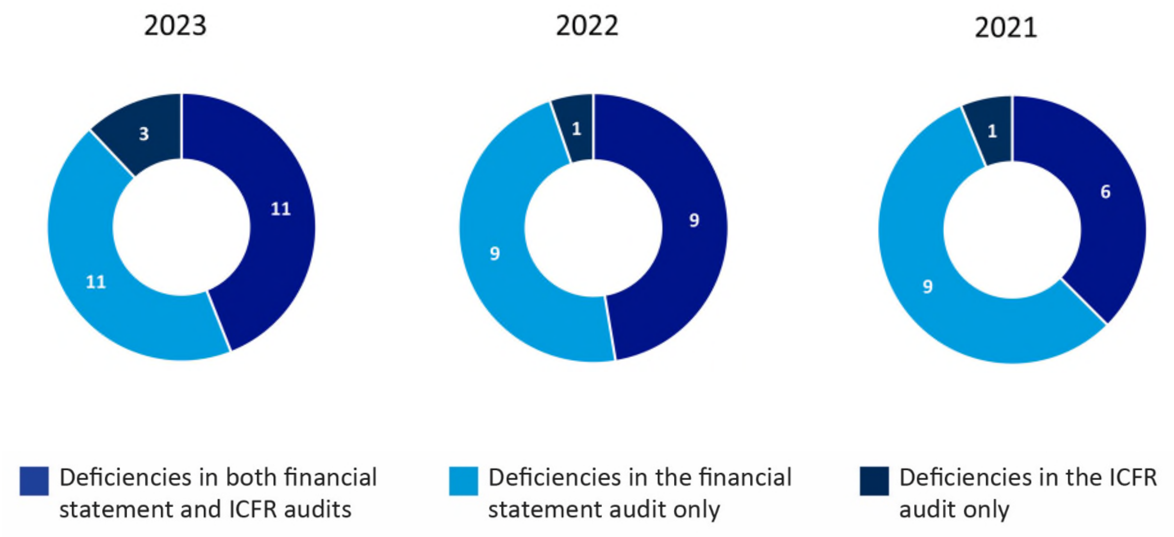


If we include a deficiency in Part I.A of our report, it does not necessarily mean that the firm has not addressed the deficiency. In many cases, the firm has performed remedial actions after the deficiency was identified. Depending on the circumstances, remedial actions may include performing additional audit procedures, informing management of the issuer of the need for changes to the financial statements or reporting on ICFR, or taking steps to prevent reliance on prior audit reports.

Our inspection may include a review, on a sample basis, of the adequacy of a firm's remedial actions, either with respect to previously identified deficiencies or deficiencies identified during the current inspection. If a firm does not take appropriate actions to address deficiencies, we may criticize its system of quality control or pursue a disciplinary action.

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

Audits Affected by the Deficiencies Identified in Part I.A



In connection with our 2023 inspection procedures for one audit, the issuer restated its financial statements to correct misstatements, and the firm revised and reissued its report on the financial statements. In addition, in connection with our 2023 inspection procedures for another audit, the issuer revised its report on ICFR, and the firm revised its opinion on the effectiveness of the issuer's ICFR to express an adverse opinion and reissued its report.

In connection with our 2022 inspection procedures for one audit, the issuer restated its financial statements to correct misstatements, and the firm revised and reissued its report on the financial statements. In addition, in connection with our 2022 inspection procedures for two other audits, the issuer corrected a misstatement in a disclosure or an omission of a required disclosure in a subsequent filing. Our 2022 inspection procedures also involved one audit for which the issuer, unrelated to our review, revised its report on ICFR and the firm revised its opinion on the effectiveness of the issuer's ICFR to express an adverse opinion and reissued its report.

Our 2021 inspection procedures involved one audit of an issuer that was formed by a merger between a non-public operating company and a special purpose acquisition company (SPAC) for which the issuer, unrelated to our review, restated its financial statements to correct a misstatement and the firm revised and reissued its report on the financial statements.

The following tables and graphs summarize inspection-related information, by inspection year, for 2023 and the previous two inspections. We caution against making any comparison of the data provided without reading the descriptions of the underlying deficiencies in each respective inspection report.

Most Frequently Identified Part I.A Deficiencies

Deficiencies in audits of financial statements	Audits with Part I.A deficiencies		
	2023	2022	2021
Did not perform sufficient testing related to a significant account or disclosure or to address an identified risk	13	9	5
Did not perform sufficient testing of data or reports used in the firm's substantive testing	9	12	2
Did not sufficiently test an estimate	9	8	2

Deficiencies in ICFR audits	Audits with Part I.A deficiencies		
	2023	2022	2021
Did not identify and test any controls that addressed the risks related to a significant account or relevant assertion	13	8	4
Did not perform sufficient testing of the design and/or operating effectiveness of controls selected for testing	9	7	5
Did not identify and/or sufficiently test controls over the accuracy and completeness of data or reports that the issuer used in the operation of controls	8	7	5

Audit Areas Most Frequently Reviewed

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

2023			2022			2021		
Audit area	Audits reviewed	Audits with Part I.A deficiencies	Audit area	Audits reviewed	Audits with Part I.A deficiencies	Audit area	Audits reviewed	Audits with Part I.A deficiencies
Revenue and related accounts	21	12	**Revenue and related accounts**	23	13	**Revenue and related accounts**	17	6
Inventory	10	7	**Goodwill and intangible assets**	9	3	**Business combinations**	8	0
Goodwill and intangible assets	9	3	**Business combinations**	8	4	**Cash and cash equivalents**	8	1
Business combinations	5	5	**Inventory**	8	3	**Equity and equity-related transactions**	7	2
Investment securities	4	2	**Equity and equity-related transactions**	5	2	**Going concern**	6	0

Audit Areas with Frequent Part I.A Deficiencies

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

Audit area	2023		2022		2021	
	Audits with Part I.A deficiencies	Audits reviewed	Audits with Part I.A deficiencies	Audits reviewed	Audits with Part I.A deficiencies	Audits reviewed
Revenue and related accounts	12	21	13	23	6	17
Inventory	7	10	3	8	1	2
Business combinations	5	5	4	8	0	8
Goodwill and intangible assets	3	9	3	9	0	4
Expenses	0	3	1	1	4	5

Revenue and related accounts: The deficiencies in 2023, 2022, and 2021 primarily related to substantive testing of, and testing controls over, revenue and related accounts.

Inventory: The deficiencies in 2023 and 2021 primarily related to substantive testing of, and testing controls over, inventory. The deficiencies in 2022 related to the accuracy and completeness of data or reports used in substantive testing and testing controls over inventory.

Business combinations: The deficiencies in 2023 primarily related to substantive testing of, and testing controls over, significant assumptions used by the issuer to determine the fair values of assets acquired in a business combination. The deficiencies in 2022 primarily related to substantive testing of significant assumptions used by the issuer to determine the fair values of assets acquired and liabilities assumed in a business combination.

Goodwill and intangible assets: The deficiencies in 2023 primarily related to evaluating intangible assets for possible impairment. The deficiencies in 2022 related to substantive testing of, and testing controls over, assumptions used by the issuer in evaluating goodwill and intangible assets for possible impairment.

Expenses: The deficiencies in 2022 related to substantive testing of expenses, including deficiencies in evaluating the appropriateness of the issuer's accounting for expenses. The deficiencies in 2021 primarily related to substantive testing of expenses, including deficiencies in substantive analytical procedures performed to test expenses.

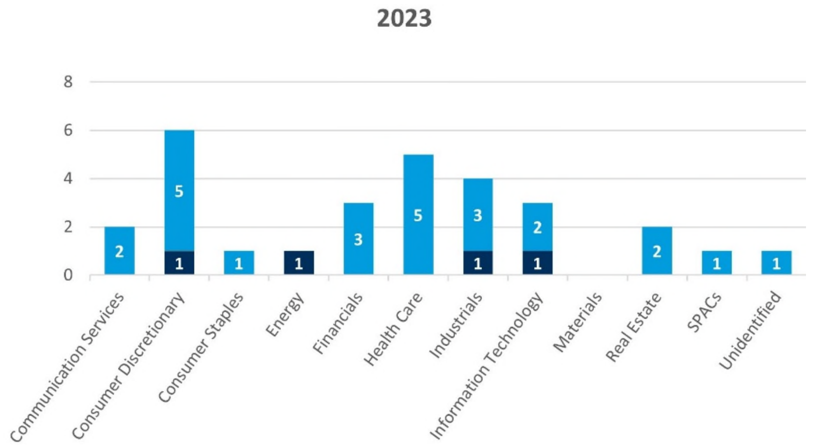
Auditing Standards Associated with Identified Part I.A Deficiencies

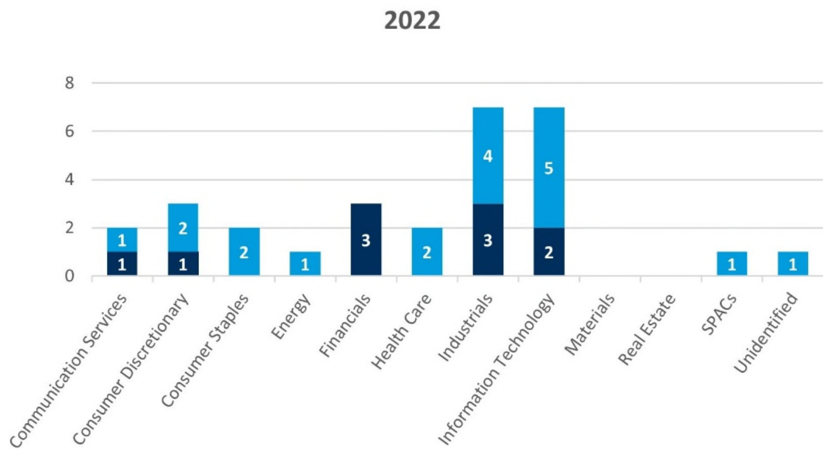
The following lists the auditing standards referenced in Part I.A of the 2023 and the previous two inspection reports, and the number of times that the standard is cited in Part I.A.

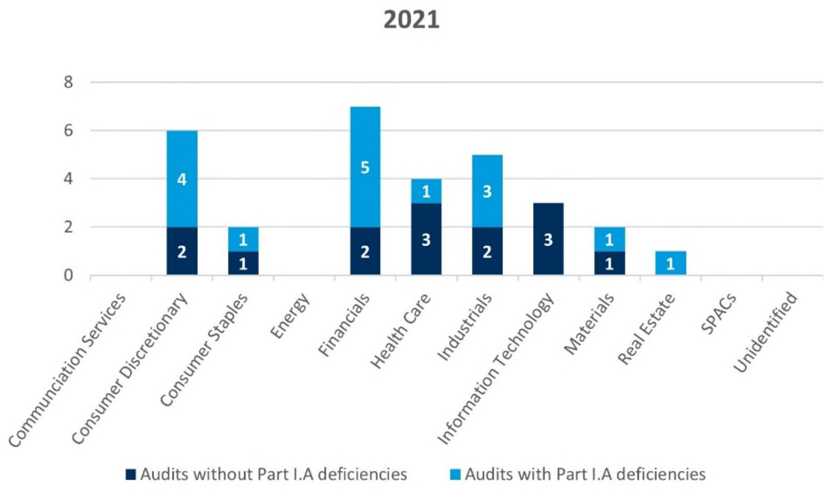
PCAOB Auditing Standards	2023	2022	2021
AS 1105, *Audit Evidence*	17	36	3
AS 1201, *Supervision of the Audit Engagement*	5	2	1
AS 1210, *Using the Work of an Auditor-Engaged Specialist*	0	1	0
AS 2101, *Audit Planning*	1	1	1
AS 2201, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*	58	55	21
AS 2301, *The Auditor's Responses to the Risks of Material Misstatement*	30	16	14
AS 2305, *Substantive Analytical Procedures*	0	1	6
AS 2310, *The Confirmation Process*	2	1	0
AS 2315, *Audit Sampling*	11	6	7
AS 2410, *Related Parties*	0	0	1
AS 2501, *Auditing Accounting Estimates, Including Fair Value Measurements* (effective for fiscal years ending on or after December 15, 2020)	14	16	1
AS 2503, *Auditing Derivative Instruments, Hedging Activities, and Investments in Securities* (effective for fiscal years ending before December 15, 2020)	-	-	2
AS 2510, *Auditing Inventories*	2	0	0
AS 2601, *Consideration of an Entity's Use of a Service Organization*	0	1	0
AS 2605, *Consideration of the Internal Audit Function*	1	0	0
AS 2810, *Evaluating Audit Results*	4	5	7

Inspection Results by Issuer Industry Sector

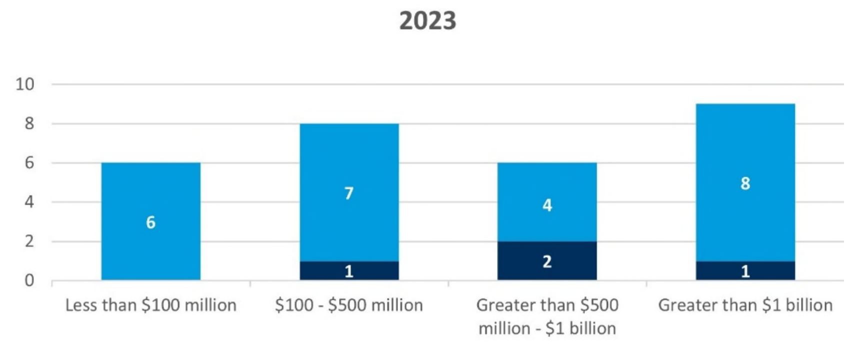
The majority of industry sector data is based on Global Industry Classification Standard (GICS) data obtained from Standard & Poor's (S&P). In instances where GICS data for an issuer is not available from S&P, classifications are assigned based upon North American Industry Classification System data. In instances where classifying an issuer using its industry sector could make an issuer identifiable, we have instead classified such issuer(s) as "unidentified."

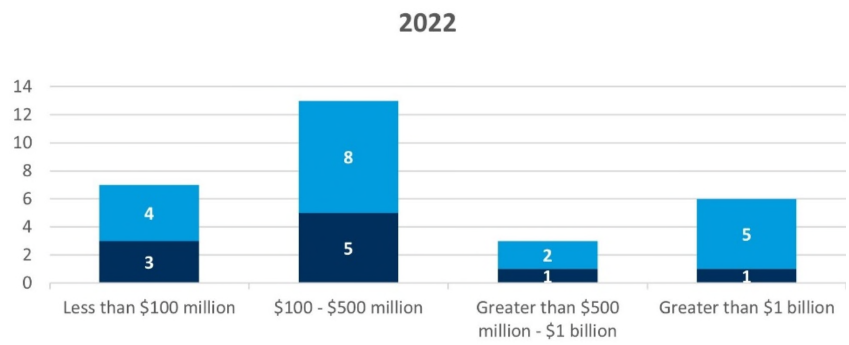


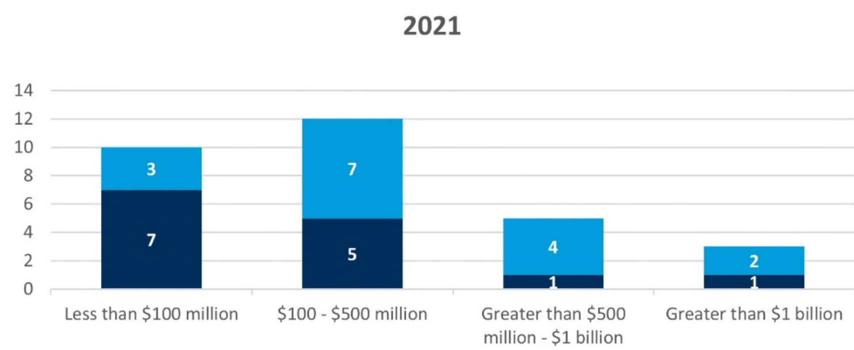




Inspection Results by Issuer Revenue Range

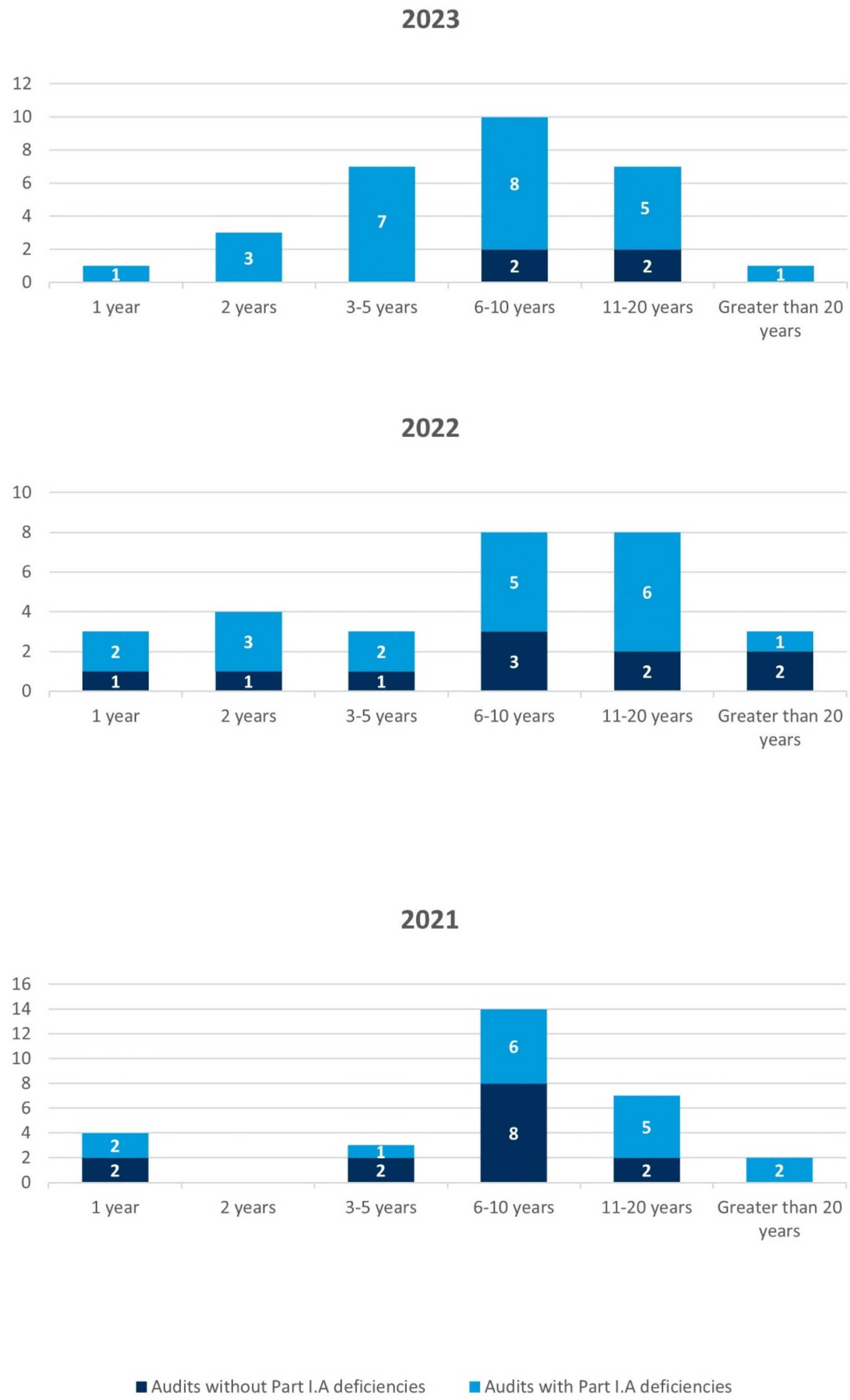




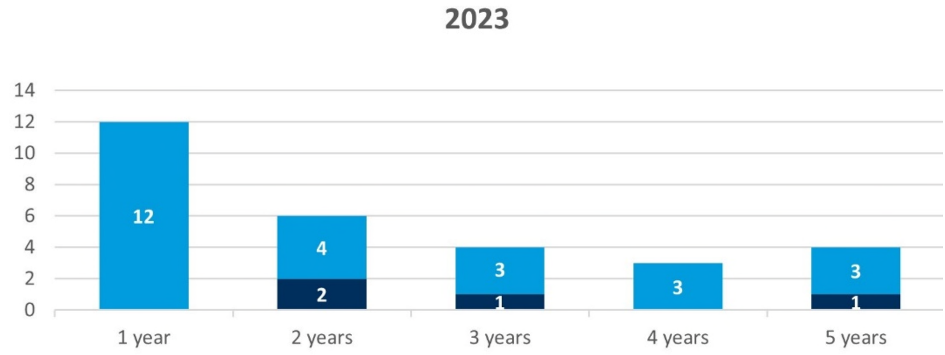


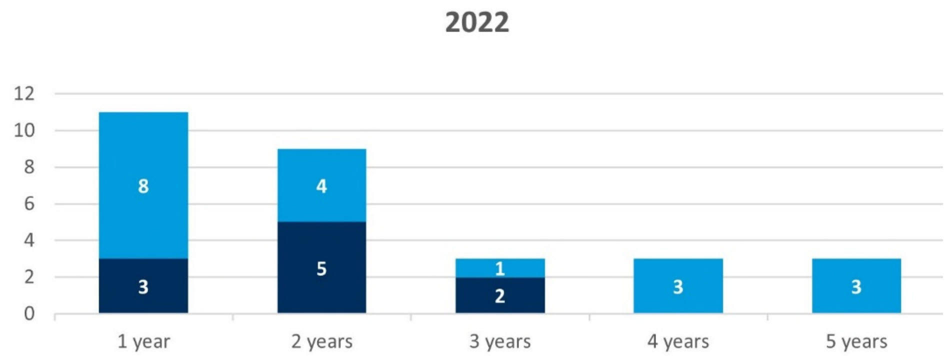
■ Audits without Part I.A deficiencies ■ Audits with Part I.A deficiencies

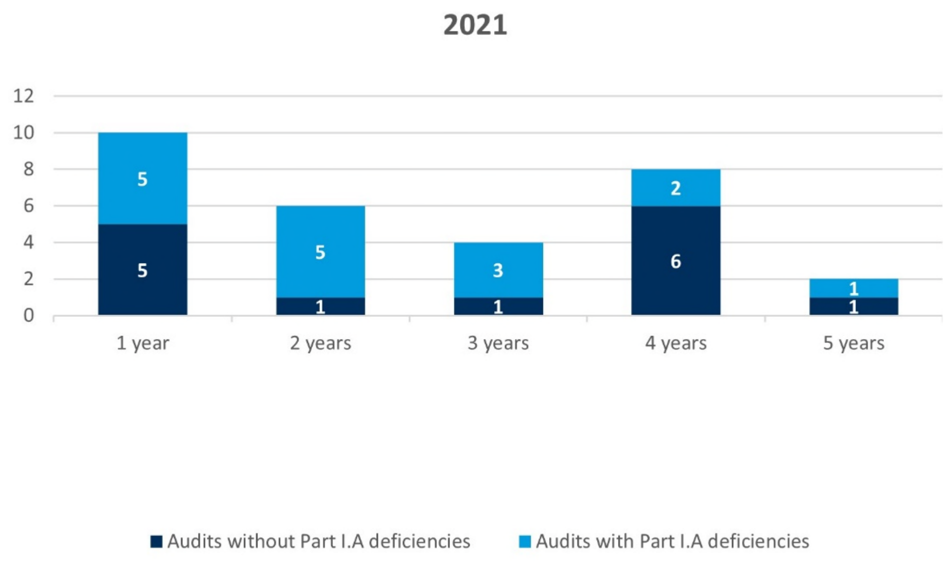
Inspection Results by the Firm's Tenure on the Issuer



Inspection Results by the Engagement Partner’s Tenure on the Issuer







Classification of Audits with Part I.A Deficiencies

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

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

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

This classification includes instances where a deficiency was identified in connection with our inspection and, as a result, an issuer's financial statements were determined to be materially misstated, and the issuer restated its financial statements. It also includes instances where a deficiency was identified in connection with our inspection and, as a result, an issuer's ICFR was determined to be ineffective, or there were additional material weaknesses that the firm did not identify, and the firm withdrew its opinion, or revised its report, on ICFR. This classification does not include instances where, unrelated to our review, an issuer restated its financial statements and/or an issuer's ICFR was determined to be ineffective. We include any deficiencies identified in connection with our reviews of these audits in the audits with multiple deficiencies or audits with a single deficiency classification below.

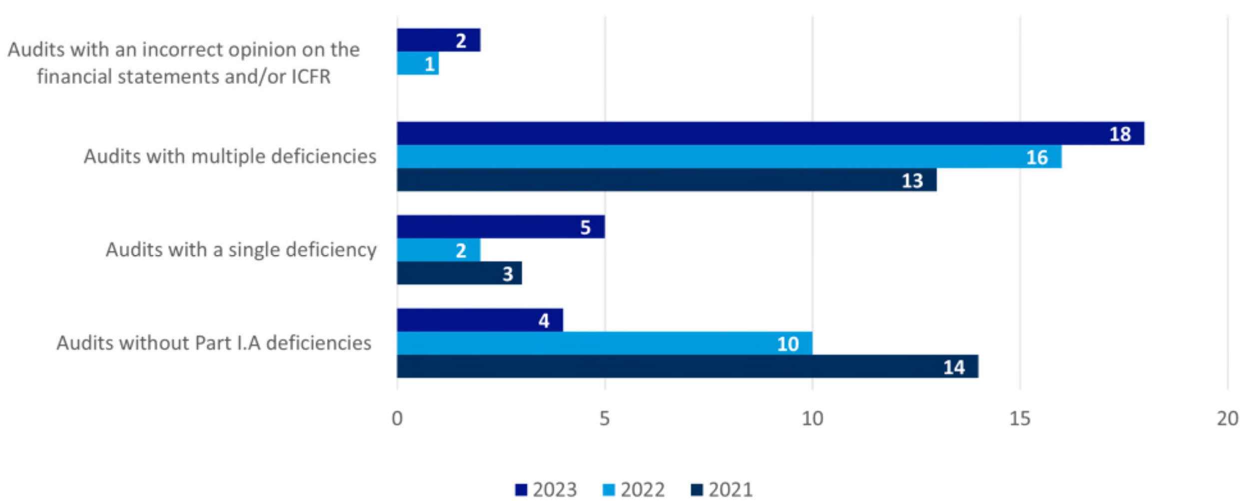
Audits with Multiple Deficiencies

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

Audits with a Single Deficiency

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

Number of Audits in Each Category



PART I: INSPECTION OBSERVATIONS

Part I.A of our report discusses deficiencies that were of such significance that we believe the firm, at the time it issued its audit report(s), had not obtained sufficient appropriate audit evidence to support its opinion(s) on the issuer's financial statements and/or ICFR.

Part I.B discusses certain deficiencies that relate to instances of non-compliance with PCAOB standards or rules other than those where the firm had not obtained sufficient appropriate audit evidence to support its opinion(s). This section does not discuss instances of potential non-compliance with SEC rules or instances of non-compliance with PCAOB rules related to maintaining independence.

Part I.C discusses instances of potential non-compliance with SEC rules or instances of non-compliance with PCAOB rules related to maintaining independence.

Consistent with the Act, it is the Board's assessment that nothing in Part I of this report deals with a criticism of, or potential defect in, the firm's quality control system. We discuss any such criticisms or potential defects in Part II. Further, you should not infer from any Part I deficiency, or combination of deficiencies, that we identified a quality control finding in Part II.

PART I.A: AUDITS WITH UNSUPPORTED OPINIONS

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

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

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

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

Issuer A – Health Care

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Revenue** and **Warrants**. The firm's internal inspection program had inspected this audit and reviewed these areas but did not identify the deficiencies below.

Description of the deficiencies identified

With respect to **Revenue**:

The issuer recorded revenue at the time its services were provided to its customers. The firm did not perform any substantive procedures to test whether the performance obligation had been fully satisfied before revenue was recognized. (AS 2301.08)

The firm used information produced by the issuer in its testing of transaction prices, but did not perform any procedures to test, or test any controls over, the accuracy and/or completeness of certain of this information. (AS 1105.10)

With respect to **Warrants**:

During the year, the issuer issued warrants that were recorded as liabilities. The firm did not identify and evaluate misstatements in the fair value measurement of these warrants. (AS 2810.30)

In connection with our review, the issuer reevaluated its accounting for these warrants and concluded that misstatements existed that had not been previously identified. The issuer subsequently corrected these misstatements in a restatement of its financial statements, and the firm revised and reissued its report on the financial statements.

Issuer B – Financials

Type of audit and related area affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Loans Receivable**, for which the firm identified a fraud risk.

Description of the deficiencies identified

The issuer held loans receivable that were measured at fair value. The issuer determined the fair values of these loans based on discounted cash flows it developed using various significant assumptions, including the issuer's approach to grouping loans in order to estimate fair value. The following deficiencies were identified:

- The firm selected for testing controls that consisted of the issuer's (1) comparison of actual cash flows to forecasted cash flows, (2) reviews of the reasonableness of discount rates, and (3) review of its disclosures related to loans receivable. The firm did not evaluate the specific review procedures that the control owners performed to identify items for follow up, investigate identified variances, and/or determine whether items identified for follow up had been appropriately resolved. (AS 2201.42 and .44) In addition, the firm did not identify and test any controls over the accuracy and completeness of certain information used in the operation of two of these controls. (AS 2201.39)

- The firm did not identify and test any controls that addressed the (1) reasonableness of the issuer's grouping of loans and (2) mathematical logic of the discounted cash flow models used by the issuer to determine the fair values of these loans. (AS 2201.39)

In connection with our review, the issuer reevaluated its controls over loans receivable and concluded that a material weakness existed that had not been previously identified. The issuer subsequently reflected this material weakness in a revision to its report on ICFR, and the firm revised its opinion on the effectiveness of the issuer's ICFR to express an adverse opinion and reissued its report.

The firm's approach for substantively testing the fair values of these loans was to test the issuer's process. The following deficiencies were identified:

- The firm did not perform any procedures to evaluate the reasonableness of the significant assumptions related to the expected timing of cash flows and the grouping of loans. (AS 2501.16)

- The firm used an auditor-employed specialist to evaluate the discount rates the issuer selected from a range of potential discount rates it developed. The firm did not identify that the work of the auditor-employed specialist did not provide sufficient appropriate audit evidence because it did not evaluate whether the issuer had a reasonable basis for (1) the discount rates used and (2) the issuer's selection of the discount rates from the range of potential discount rates. (AS 1201.C6 and .C7; AS 2501.16)

- The firm did not perform sufficient procedures to evaluate whether the method used by the issuer to develop the fair values of these loans was in conformity with the requirements of GAAP, including whether the data were appropriately used and significant assumptions were appropriately applied under GAAP, because the firm did not test the mathematical logic of the discounted cash flow models. (AS 2501.10)

The firm used an issuer-prepared schedule in its substantive testing of certain loans-receivable disclosures but did not perform any procedures to test, or test controls over, the accuracy and completeness of this schedule. (AS 1105.10)

Audits with Multiple Deficiencies

Issuer C – Consumer Staples

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Revenue**, **Accounts Receivable**, **Debt**, **Business Combinations**, **Intangible Assets**, and **Financial Reporting and Close**.

Description of the deficiencies identified

With respect to **Revenue** and **Accounts Receivable**:

The issuer offered preferred pricing based on a customer's status. The following deficiencies were identified with respect to revenue from certain of these customers:

- The firm selected for testing a control that consisted of the issuer's review of customer pricing changes subsequent to the execution, renewal, or amendment of a customer contract with preferential pricing. The number of changes selected for testing did not provide sufficient appropriate audit evidence given the frequency with which the control operated. (AS 2201.46)

- The firm selected for testing controls that included the issuer's review of customers' status. The firm did not test the aspects of these controls that addressed the issuer's review of changes to existing customers' status. (AS 2201.42 and .44)

- The firm did not identify and test any controls over the accuracy of product cost information the issuer used to determine the sales prices in accordance with certain customer contracts. (AS 2201.39)

- The firm did not perform procedures to test, or (as discussed above) test controls over, the accuracy and/or completeness of certain system-generated data or reports the firm used in its substantive testing of this revenue. (AS 1105.10)

For two business units, the firm did not identify and test any controls over the accuracy and completeness of certain information used to record revenue. (AS 2201.39)

For these same business units, the firm selected for testing certain controls that prevented the processing of orders for customers on credit hold. The firm did not test, beyond inquiry, the aspect of these controls that addressed which users had the ability to release customers from credit hold. (AS 2201.42 and .44)

For one of these business units, the firm selected for testing a control over the issuer's review of certain customer's accounts receivable balances. The firm did not identify and test any controls over the accuracy and completeness of a report used in the operation of this control. (AS 2201.39)

For two other business units, the firm did not identify and test any controls that addressed the risk of material misstatement related to the acceptance of invalid or unauthorized customer orders. (AS 2201.39)

The sample sizes the firm used in certain of its substantive procedures to test revenue were too small to provide sufficient appropriate audit evidence because these procedures were designed based on a level of control reliance that was not supported due to the deficiencies in the firm's control testing discussed above. (AS 2301.16, .18, and .37; AS 2315.19, .23, and .23A)

The firm subjected certain other of the issuer's business units to less extensive audit procedures. With respect to revenue from these business units, the following deficiencies were identified:

- In determining the extent to which audit procedures should be performed, the firm did not evaluate (1) the materiality of these business units, (2) the decentralized nature of records and information processing at these business units, and (3) whether the risks of material misstatement that the firm identified for the business units subject to more extensive audit procedures also applied to these business units. (AS 2101.11 and .12; AS 2201.B10)

- To address the risks of material misstatement related to revenue for these business units, the firm selected for testing a control that included the issuer's comparisons and reviews of the consolidated (1) budget to actual results and (2) prior-period actual results to current-period actual results. The firm did not evaluate the specific review procedures that the control owner performed to investigate identified variances and determine whether items identified for follow up had been appropriately resolved. (AS 2201.42 and .44) In addition, the firm did not identify and test any controls over the review of the budget used in the operation of this control. (AS 2201.39)

- The firm did not perform any substantive procedures to test revenue for these business units. (AS 2301.08)

With respect to **Debt**:

The firm sent positive confirmation requests to the issuer's lenders. The following deficiencies were identified related to the confirmation requests for one of the lenders:

- The firm did not maintain control over a confirmation request through direct communication between the firm and the intended recipient of the request. (AS 2310.28)
- The confirmation response was returned by email. The firm performed procedures to verify the source of the response but did not evaluate certain inconsistencies it identified through the performance of these procedures. (AS 2310.29)

The firm did not identify and test any controls that addressed the issuer's compliance with certain non-financial contractual debt covenants. (AS 2201.39) The firm did not perform any substantive procedures to test the issuer's compliance with these covenants. (AS 2301.08)

The firm used certain issuer-prepared schedules in its substantive testing of certain debt disclosures. The firm did not perform any procedures to test, or (as discussed further below) test controls over, the accuracy of these schedules. (AS 1105.10) In addition, the firm did not identify and evaluate certain differences between the issuer's debt disclosures and these schedules. (AS 2301.08)

The firm did not perform any procedures to test the issuer's fair value disclosures for certain debt. (AS 2501.07)

With respect to **Business Combinations**:

During the year, the issuer acquired multiple businesses. The following deficiencies were identified:

- The firm selected for testing a control that included the issuer's review of the fair values of assets acquired in these business combinations, including the assumptions the issuer used. In its testing of the operating effectiveness of this control, the firm did not evaluate whether an item identified for follow up was appropriately resolved. (AS 2201.44) In addition, the firm did not identify and test any controls over the accuracy and completeness of certain data used in the operation of this control. (AS 2201.39)
- For one of these business combinations, the firm did not sufficiently evaluate whether an assumption was consistent with historical and recent experience because it did not evaluate the significant differences between the assumption and this experience. Further, when evaluating the issuer's ability to carry out its planned course of action, the firm performed a sensitivity analysis for this assumption but did not evaluate the significant differences between the alternative assumptions it used in this analysis and the issuer's historical and recent experience. (AS 2501.16 and .17)
- The firm did not identify and evaluate a misstatement in a required disclosure under FASB ASC Topic 805, *Business Combinations*. (AS 2810.30 and .31)

With respect to **Intangible Assets**:

The firm did not identify and test any controls that addressed whether the issuer used appropriate useful lives in the calculation of amortization expense for finite-lived intangible assets. (AS 2201.39)

The firm did not identify and evaluate a misstatement in a required disclosure under FASB ASC Topic 350, *Intangibles – Goodwill and Other*. (AS 2810.30 and .31)

With respect to **Financial Reporting and Close**, for which the firm identified a fraud risk:

The firm did not identify and test any controls over the accuracy of certain schedules the issuer used to determine its financial statement disclosures. (AS 2201.39)

The firm selected for testing a control that was designed to address the firm's identified fraud risk related to inappropriate changes being made to certain business unit sub-ledgers prior to consolidation. In its testing of the operating effectiveness of this control, the firm did not evaluate the specific review procedures that the control owner performed to investigate identified differences. (AS 2201.44) In addition, the firm did not identify and test any controls over the accuracy and completeness of certain business unit sub-ledgers used in the operation of the control. (AS 2201.39)

The firm's substantive procedures to address the risk related to inappropriate changes consisted of an independent comparison of certain business unit sub-ledgers to the general ledger. The following deficiencies were identified:

- The firm (1) limited its comparison to certain accounts and (2) identified differences in its testing of these accounts but did not perform procedures to evaluate these differences, other than concluding that the differences were not material in the aggregate. (AS 2301.13)
- The firm did not perform procedures to test, or (as discussed above) test controls over, the accuracy and completeness of the business unit sub-ledgers it used in its testing. (AS 1105.10)

The firm identified a fraud risk related to the potential for management to override controls, including recording unsupported journal entries. For the business units the firm subjected to less extensive audit procedures, the following deficiencies were identified:

- The firm did not identify and test any controls that addressed this risk. (AS 2201.39)
- The firm did not perform any substantive procedures to test journal entries to address this risk. (AS 2401.58)

Issuer D – Information Technology

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Revenue and Related Accounts**, **Inventory**, and **Journal Entries**.

Description of the deficiencies identified

With respect to **Revenue and Related Accounts**, for which the firm identified a significant risk:

The issuer recorded revenue net of customer sales incentives and returns. The following deficiencies were identified with respect to one business unit:

- The firm selected for testing a control that consisted of the issuer's review of the sales incentive reserve. The firm did not evaluate the specific review procedures that the control owner performed to assess the (1) reasonableness of the sales incentive reserve and (2) accuracy and completeness of certain information used to determine the sales incentive reserve. (AS 2201.42 and .44)

- The firm selected for testing a control that consisted of the issuer's review of sales returns. The firm did not identify and test any controls over the accuracy and completeness of return information used in the operation of this control. (AS 2201.39)
- The firm did not perform any procedures to test, or test controls over, the accuracy and completeness of a report produced by the issuer that it used in its substantive testing of the sales incentive reserve. (AS 1105.10)
- The firm's approach to substantively test the issuer's sales return reserve was to develop an independent expectation of the estimate. The firm did not perform procedures to demonstrate it had a reasonable basis for the method used to develop its independent expectation. (AS 2501.22)

The firm selected for testing a control over the issuer's review of the accuracy of pricing information used to record revenue at this business unit. The firm did not identify and test any controls over the accuracy of certain information used in the operation of this control. (AS 2201.39)

The sample sizes the firm used in certain of its substantive procedures to test revenue and related accounts at this business unit were too small to provide sufficient appropriate audit evidence because these procedures were designed based on a level of control reliance that was not supported due to the deficiencies in the firm's control testing discussed above. (AS 2301.16, .18, and .37; AS 2315.19, .23, and .23A)

For a second business unit, the firm's approach to substantively test the issuer's sales incentive and sales return reserves was to examine transactions that occurred after year end. The firm did not evaluate whether the audit evidence obtained was sufficient, including whether the evidence supported or contradicted these estimates. (AS 2501.28)

With respect to **Inventory**:

The firm selected for testing a control over the issuer's review of the reserve for excess and obsolete inventory at one business unit. The firm did not identify and test any controls over the accuracy and completeness of certain information used in the operation of this control. (AS 2201.39)

With respect to **Journal Entries**, for which the firm identified a fraud risk:

The firm identified a fraud risk related to the potential for management to override controls, including recording unsupported journal entries. The firm subjected certain of the issuer's business units to less extensive audit procedures. The firm did not perform any substantive procedures to test journal entries to address this risk at these business units. (AS 2401.58)

Issuer E – Industrials

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Revenue**, **Accounts Receivable**, **Inventory**, **Accounts Payable**, and **Journal Entries**. The firm's internal inspection program had inspected this audit and reviewed the Information Technology General Controls (ITGCs) area but did not identify the deficiency below.

Description of the deficiencies identified

With respect to **Revenue**, for which the firm identified a fraud risk, **Accounts Receivable**, **Inventory**, and **Accounts Payable**:

For one business unit, the issuer used an information-technology (IT) system to initiate, process, and record transactions related to revenue, accounts receivable, inventory, and accounts payable. In its testing of controls over these accounts, the firm tested various automated and IT-dependent manual controls that used data and reports generated or maintained by this IT system. The firm did not identify and test any controls that addressed the risk that certain unauthorized changes were made to this system. (AS 2201.39) As a result of this deficiency in the firm's testing of ITGCs, the firm's testing of these automated and IT-dependent manual controls was not sufficient. (AS 2201.46)

As a result of the firm's ITGC testing deficiency discussed above, the firm did not perform sufficient other audit procedures, as follows:

- For certain revenue, accounts receivable, and inventory, the firm did not perform sufficient procedures to test, or sufficiently test controls over, the accuracy and/or completeness of certain system-generated data or reports the firm used (1) to make its selections to test certain controls and (2) in its substantive testing. (AS 1105.10)
- The sample sizes the firm used in certain of its substantive procedures to test certain revenue and accounts receivable were too small to provide sufficient appropriate audit evidence because these procedures were designed based on a level of control reliance that was not supported. (AS 2301.16, .18, and .37; AS 2315.19, .23, and .23A)

With respect to **Inventory**:

For inventory at three business units, one of which was affected by the audit deficiencies discussed above, the following (additional) deficiencies were identified:

- The firm did not identify and test any controls over inventory costing. (AS 2201.39)
- The firm selected for testing controls that consisted of the issuer's performance of physical inventory counts. The firm did not test the aspect of these controls that addressed whether recorded inventory reflected the results of the issuer's physical counts. (AS 2201.42 and .44)
- The firm did not perform sufficient procedures to test the existence of this inventory because it did not inspect any records of the issuer's counts on which the year-end inventory was based. (AS 2301.08)
- The sample sizes the firm used in certain of its substantive procedures to test inventory were too small to provide sufficient appropriate audit evidence because these procedures were designed based on a level of control reliance that was not supported due to the deficiencies in the firm's control testing discussed above. (AS 2301.16, .18, and .37; AS 2315.19, .23, and .23A)

With respect to **Journal Entries**, for which the firm identified a fraud risk:

The firm identified a fraud risk related to the potential for management to override controls, including recording unsupported journal entries. The firm subjected certain of the issuer's business units to less extensive audit procedures. With respect to these business units, the following deficiencies were identified:

- The firm did not identify and test any controls that addressed this risk. (AS 2201.39)
- The firm did not perform any substantive procedures to test journal entries to address this risk. (AS 2401.58)

Issuer F – Industrials

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Revenue**, **Inventory**, and **Business Combinations**.

Description of the deficiencies identified

With respect to **Revenue**, for which the firm identified a fraud risk:

For one business unit, the firm's substantive procedures to test revenue consisted of testing a sample of transactions. For certain of the transactions it selected for testing, the firm was unable to obtain evidence demonstrating that the performance obligation had been satisfied when revenue was recognized. The firm did not consider the effect of these unexamined transactions on its evaluation of the sample results. (AS 2315.25)

For a second business unit, the following deficiencies were identified:

- The firm did not identify and test any controls that addressed the risk related to accuracy of the quantity of items ordered. (AS 2201.39)
- The sample size the firm used in its substantive procedures to test this revenue was too small to provide sufficient appropriate audit evidence because these procedures were designed based on a level of control reliance that was not supported due to the deficiency in the firm's control testing discussed above. (AS 2301.16, .18, and .37; AS 2315.19, .23, and .23A)

With respect to **Inventory**:

For one business unit, the firm selected for testing the issuer's cycle-count control over the existence of inventory. The firm did not evaluate whether this control was designed to address whether all recorded inventory items were counted. (AS 2201.42)

Due to the deficiency discussed above, the firm did not obtain sufficient appropriate audit evidence that the cycle-count procedures the issuer used for this inventory were sufficiently reliable to produce results substantially the same as those that would have been obtained by a count of all items each year. (AS 2510.11)

For another business unit, the issuer performed full physical counts of inventory at various locations before year end. To test the existence of inventory at these locations, the firm observed the issuer's physical counts and made certain independent test counts. The following deficiencies were identified:

- For one of these locations, the firm obtained an inventory listing from a date subsequent to the issuer's physical count. The firm did not inspect any records of the issuer's counts and apply appropriate tests of intervening transactions between the date of the issuer's counts and the date of the inventory listing. (AS 2510.12)
- For another location, the firm did not perform any procedures to evaluate certain differences it identified from its independent test counts. (AS 2301.08)
- For the above locations and certain other locations, the firm did not perform appropriate procedures to test, or test controls over, the accuracy and/or completeness of certain issuer-produced reports it used to test intervening transactions between the dates of its inventory observations and year end. (AS 1105.10)

With respect to **Business Combinations**:

During the year, the issuer acquired several businesses. The firm selected for testing a control that included the issuer's review of the fair values of assets acquired in these business combinations, including the significant assumptions used. The firm did not evaluate the specific review procedures the control owner performed to assess the reasonableness of certain significant assumptions. (AS 2201.42 and .44) In addition, the firm did not identify and test any controls over the accuracy and completeness of certain data used in the operation of this control. (AS 2201.39)

For one of these business combinations, the issuer engaged a specialist to assist it in determining the fair values of certain acquired intangible assets using various significant assumptions developed by the issuer or the company's specialist. The following deficiencies were identified:

- The firm used an auditor-employed specialist to evaluate the reasonableness of a significant assumption developed by the company's specialist that was used in the measurement of an acquired intangible asset. The firm did not identify that the work of the auditor-employed specialist did not provide sufficient appropriate audit evidence because the auditor-employed specialist did not evaluate (1) whether this assumption was consistent with recent existing market information and (2) whether certain data the company's specialist used to develop this assumption were relevant to the assumption, beyond observing that the data were from comparable industries. (AS 1105.A8a and .A8b; AS 1201.C6 and .C7)
- The firm's approach for substantively testing the fair value of another acquired intangible asset was to test the issuer's process. The firm did not sufficiently evaluate whether the issuer had a reasonable basis for a significant assumption it developed because it did not evaluate the (1) issuer's exclusion of certain historical experience and (2) appropriateness of certain data that the issuer used to develop this assumption. (AS 2501.16)

For this business combination, the firm did not perform any substantive procedures to test the existence of inventory at the acquisition date. (AS 2301.08)

Issuer G – Financials

Type of audit and related areas affected

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

Description of the deficiencies identified

With respect to **Investments**:

The issuer used various service organizations for the custody, recordkeeping, and processing of certain investment transactions, and these service organizations used sub-service organizations for certain functions. The firm obtained the service auditor's reports for each of these service organizations and identified certain complementary user controls that the service auditor's reports described as necessary. The following deficiencies were identified:

- The firm selected for testing a control that addressed the issuer's review of investment pricing. The firm did not evaluate whether the control was designed to satisfy the control objective given that certain investments were excluded from this control. (AS 2201.42 and .B22)
- The firm selected for testing a control that addressed the issuer's review of certain investments for potential impairment. The firm did not evaluate whether the control was designed to consider all of the relevant requirements of FASB ASC Topic 326, *Current Expected Credit Losses*, when assessing whether an impairment loss or credit impairment existed for these investments. (AS 2201.42 and .B22)
- The firm selected for testing a control over the review of monthly investment reconciliations. The firm did not identify and test any controls over the accuracy and completeness of certain reports used in the operation of this control. (AS 2201.39)
- The firm did not obtain an understanding of, or test, any relevant controls at certain sub-service organizations. (AS 2201.39 and .B19)
- For one sub-service organization, the firm did not perform any procedures to evaluate whether there were any changes in the sub-service organization's controls from the date of the service auditor's report to year end given the length of period under audit not covered by the service auditor's report. (AS 2201.B24 and .B25)

The sample size the firm used in certain of its substantive procedures to test these investments was too small to provide sufficient appropriate audit evidence because these procedures were designed based on a level of control reliance that was not supported due to deficiencies in the firm's control testing discussed above. (AS 2301.16, .18, and .37; AS 2315.19, .23, and .23A)

The firm did not perform sufficient procedures to evaluate the issuer's conclusion that no impairment or credit loss existed for certain investments because it did not take into account certain relevant requirements of FASB ASC Topic 326. (AS 2301.08)

The firm used an auditor-engaged specialist to assist it with evaluating the appropriateness of the issuer's categorization of investments within the fair value hierarchy set forth in FASB ASC Topic 820, *Fair Value Measurement*. The firm identified certain differences between the categorizations determined by the issuer and those determined by the auditor-engaged specialist but did not perform any procedures to evaluate these differences. (AS 2301.08)

With respect to **Liabilities for Insurance Reserves**, for which the firm identified a significant risk:

The issuer used an IT system to process and record transactions and data, which the issuer used in estimating its insurance reserves. The firm selected for testing controls over change management for this system but did not perform any procedures to test, or test any controls over, the completeness of the population of items from which it selected its samples for testing. (AS 1105.10)

In its testing of controls over insurance reserves, the firm tested various IT-dependent manual controls that used data generated or maintained by this IT system. As a result of the above deficiency in the firm's testing of ITGCs, the firm's testing of these IT-dependent controls was not sufficient. (AS 2201.46) In addition, the firm did not identify and test any controls over the reliability of certain data that the issuer obtained from external parties and used in the operation of these IT-dependent controls. (AS 2201.39)

The firm's approach for substantively testing insurance reserves was to develop an independent expectation using these external data. The firm did not evaluate the reliability of these data used in developing its independent expectation. (AS 1105.04 and .06)

Issuer H

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Revenue**, **Inventory**, and **Accounts Payable**. This was the firm's initial audit of this issuer.

Description of the deficiencies identified

The firm used the work of internal audit as evidence of the effectiveness of certain controls over revenue, inventory, and accounts payable that the firm selected for testing. The firm identified that certain individuals from internal audit also served as control owners for certain of these controls. The firm did not sufficiently assess the objectivity of internal audit because it did not determine whether these individuals participated in the audit of these controls. (AS 2201.18; AS 2605.10)

With respect to **Inventory**:

The issuer performed cycle counts of certain inventory. The firm selected for testing controls that consisted of the issuer's review of the cycle-count results. The following deficiencies were identified:

- For one of these controls, the firm did not test, beyond inquiry, certain aspects of this control. Further, in evaluating the design of another aspect of this control, the firm did not determine whether certain items identified for follow up were appropriately resolved. (AS 2201.42 and .44)
- In evaluating the design of an aspect of another control, the firm did not evaluate whether the thresholds the control owner used to identify items for investigation were sufficiently precise to detect material misstatements. (AS 2201.42) In addition, the firm did not identify and test any controls over the accuracy of certain information used in the operation of the control. (AS 2201.39)

To test the existence of this inventory, the firm performed independent physical counts of inventory at year end. The following deficiencies were identified:

- The firm did not sufficiently test inventory because it did not compare the inventory listings it used to perform its substantive procedures to the recorded balance. (AS 2301.08)
- The firm's sample size for testing the existence of this inventory was too small to provide sufficient appropriate audit evidence because, in determining the sample size, the firm did not

take into account tolerable misstatement and the allowable risk of incorrect acceptance. (AS 2315.16, .23, and .23A)

For certain inventory, the firm did not identify and test any controls over the reserve for excess and obsolete inventory. (AS 2201.39)

The firm's substantive procedures to test the cost of certain inventory consisted of selecting a sample of items for testing. The sample size the firm used was too small to provide sufficient appropriate audit evidence because these procedures were designed based on a level of control reliance that was not supported, as it did not take into account that one of the controls it relied upon was ineffective. (AS 2301.16, .18, and .37; AS 2315.19, .23, and .23A)

Issuer I – Health Care

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Revenue and Related Accounts**, a **Business Combination**, and **Intangible Assets**.

Description of the deficiencies identified

With respect to **Revenue and Related Accounts**, for which the firm identified a fraud risk:

The issuer used service organizations to process and/or record transactions for revenue and related accounts, and the firm used certain information, including delivery information, produced by these service organizations in its substantive testing of these accounts. The following deficiencies were identified:

- The firm did not perform any procedures to test the accuracy and/or completeness of certain of this information. (AS 2301.08 and .13)
- The firm's substantive procedures to test revenue included selecting a sample of revenue transactions. For certain selections, the firm did not perform substantive procedures to test this delivery information, beyond comparing the information to another report from the service organization. (AS 2301.08 and .13)

With respect to a **Business Combination**, for which the firm identified a significant risk:

During the year, the issuer acquired a business and determined the fair value of an acquired intangible asset using forecasted cash flows, which included significant assumptions related to sales growth, product mix, and pricing for the forecast period. The following deficiencies were identified:

- The firm did not perform any procedures to evaluate the reasonableness of the forecasted sales growth. (AS 2501.16)
- The firm did not sufficiently evaluate the reasonableness of certain pricing assumptions because it limited its procedures to inquiry of management and review of internal plans, without taking into account the issuer's ability to carry out its planned course of action. (AS 2501.16 and .17)
- The firm did not evaluate whether the issuer had a reasonable basis for (1) the product mix assumption and (2) another pricing assumption. (AS 2501.16)

With respect to **Intangible Assets**:

The firm did not perform procedures to evaluate certain indicators of potential impairment that existed at year end. (AS 2301.08)

Issuer J – Communication Services

Type of audit and related area affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Revenue**, for which the firm identified a fraud risk.

Description of the deficiencies identified

For certain revenue at one business unit, the following deficiencies were identified:

- For contracts with recurring monthly revenue, the firm did not identify and test any controls over the recording of certain of this revenue. (AS 2201.39)
- The firm selected for testing a control that included the issuer's review of the accuracy and completeness of customer contract information in the issuer's system that it used to record revenue. In its testing of the operating effectiveness of this control, the firm did not test this aspect of the control. (AS 2201.44)
- As a result of the deficiency discussed above, the firm did not perform sufficient procedures to test, or sufficiently test controls over, the completeness of a report used in its substantive testing. (AS 1105.10)

For certain revenue at two other business units, the firm selected for testing controls that addressed whether the performance obligation had been satisfied before revenue was recognized. The number of occurrences selected for testing did not provide sufficient appropriate audit evidence in light of either the assessed inherent risk associated with the account or the frequency of the operation of the control. (AS 2201.46)

For one of these two business units, the firm did not perform any substantive procedures to test whether the performance obligation was satisfied before revenue was recognized for the first 10 months of the year. (AS 2301.08)

The sample sizes the firm used in certain of its substantive procedures to test revenue were too small to provide sufficient appropriate audit evidence because (1) these procedures were designed based on a level of control reliance that was not supported due to the deficiencies in the firm's control testing discussed above and/or (2) in determining the sample size, the firm did not take into account the allowable risk of incorrect acceptance. (AS 2301.16, .18, and .37; AS 2315.16, .19, .23, and .23A)

Issuer K – Consumer Discretionary

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Revenue** and a **Business Combination**.

Description of the deficiencies identified

With respect to **Revenue**:

The issuer used a service organization to accumulate revenue data initiated in and processed by the issuer's various IT systems and the issuer recorded certain revenue based on these data. The following deficiencies were identified:

- The firm did not identify and test any controls over the accuracy and completeness of the revenue data that had been accumulated by the service organization from the various IT systems. (AS 2201.39)
- The firm did not perform procedures to test, or (as discussed above) identify and test controls over, the accuracy and/or completeness of certain of these data that the firm used in its substantive testing of this revenue. (AS 1105.10)
- The sample size the firm used in its substantive procedures to test certain of this revenue was too small to provide sufficient appropriate audit evidence because these procedures were designed based on a level of control reliance that was not supported due to the deficiency in the firm's control testing discussed above. (AS 2301.16, .18, and .37; AS 2315.19, .23, and .23A)

With respect to a **Business Combination**:

During the year, the issuer acquired a business. The firm selected for testing a control that included the issuer's review of the valuation of acquired intangible assets and related assumptions. The firm did not identify and test any controls over the accuracy and completeness of certain data used in the operation of this control. (AS 2201.39)

Issuer L – Communication Services

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Revenue** and **Journal Entries**.

Description of the deficiencies identified

With respect to **Revenue**, for which the firm identified a fraud risk:

The issuer recognized certain revenue based on customer activity that was tracked using the issuer's various IT systems, and it used service organizations to process customer payments. The firm's approach for substantively testing certain of this revenue consisted primarily of performing a software-assisted analysis to test the relationships between revenue and cash receipts. The reliability of the audit evidence obtained from this analysis was dependent upon the firm's testing of the underlying data. The firm did not sufficiently test the accuracy of the underlying data because the firm did not perform any procedures to (1) test, or test controls over, certain internally generated information that it used and (2) test the issuer's complementary user controls that the service auditor's reports described as necessary to rely on this payment information. (AS 1105.10; AS 2301.08 and .13)

With respect to **Journal Entries**, for which the firm identified a fraud risk:

To identify and select journal entries for testing, the firm identified fraud characteristics and obtained a list of all journal entries with these characteristics. The firm did not perform sufficient procedures to test those journal entries because it examined the underlying support for only certain journal entries, without having an appropriate rationale for limiting its testing to those certain journal entries. (AS 2401.61)

Issuer M – Health Care

Type of audit and related area affected

In our review, we identified deficiencies in the financial statement audit related to **Derivatives**, for which the firm identified a significant risk.

Description of the deficiencies identified

During the year, the issuer entered into a convertible debt agreement that included an embedded conversion option; the issuer accounted for this option as a derivative liability. The following deficiencies were identified:

- The issuer engaged a specialist to determine the fair value of this liability at issuance. The firm's approach for substantively testing the fair value of this liability at issuance was to test the issuer's process, and the firm used an auditor-employed specialist to evaluate a significant assumption the company's specialist developed using a range of potential assumptions from comparable companies. The firm did not identify that the work of the auditor-employed specialist did not provide sufficient appropriate audit evidence because the auditor-employed specialist's procedures were limited to determining that the assumption was among the higher end of the range of potential assumptions. (AS 1105.A8b; AS 1201.C6 and .C7)
- The firm did not identify and evaluate misstatements in the financial statements and required disclosures related to this derivative liability. (AS 2810.30 and .31)

Issuer N – Real Estate

Type of audit and related area affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to **Income Taxes**.

Description of the deficiencies identified

The firm did not identify and test any controls that addressed the risk related to the issuer's compliance with transfer pricing regulations for intercompany transactions. (AS 2201.39)

The firm did not perform any substantive procedures to evaluate the issuer's assessment of its compliance with transfer-pricing regulations for intercompany transactions. (AS 2301.08)

Issuer O – Financials

Type of audit and related areas affected

In our review, we identified deficiencies in the financial statement audit related to **Investments** and **Journal Entries**.

Description of the deficiencies identified

With respect to **Investments:**

The firm used an auditor-engaged specialist to assist it with evaluating the appropriateness of the issuer's categorization of investments within the fair value hierarchy set forth in FASB ASC Topic 820. The firm identified a difference between the categorization determined by the issuer and determined by the auditor-engaged specialist but did not perform any procedures to evaluate this difference. (AS 2301.08)

With respect to **Journal Entries**, for which the firm identified a fraud risk:

To identify and select journal entries for testing, the firm identified fraud characteristics. The firm did not perform any procedures to evaluate whether any of the journal entries recorded in the last month of the year had these characteristics. (AS 2401.61 and .62)

Issuer P – Industrials

Type of audit and related area affected

In our review, we identified deficiencies in the financial statement and ICFR audits related to a **Business Combination**.

Description of the deficiencies identified

During the year, the issuer acquired a business and engaged a specialist to assist it in determining the fair values of certain acquired assets. The firm selected for testing a control that included the issuer's comparison of fair values determined by the company's specialist to fair values included in a separate valuation report received by the issuer. The firm did not identify and test any controls over the reasonableness of the fair values included in the separate valuation report used in the operation of this control. (AS 2201.39)

The firm used an auditor-employed specialist to assist it with testing the fair values of these acquired assets, which were determined by the company's specialist. The auditor-employed specialist's approach consisted of developing independent expectations consisting of a range of the fair values for a selection of these assets. The firm did not identify that the work of the auditor-employed specialist did not provide sufficient appropriate audit evidence because it did not evaluate whether the independent expectations of the fair values as a range encompassed only reasonable outcomes and were supported by sufficient appropriate audit evidence. (AS 1201.C6 and .C7; AS 2501.25)

Issuer Q – Consumer Discretionary

Type of audit and related area affected

In our review, we identified deficiencies in the ICFR audit related to **Revenue**, for which the firm identified a fraud risk.

Description of the deficiencies identified

The issuer recorded revenue net of customer rebates and other deductions. The following deficiencies were identified:

- The firm selected for testing a control that consisted of the issuer's review of the reconciliation between net revenue and cash receipts. The firm did not evaluate the specific review procedures that the control owner performed to assess certain adjustments between net revenue and cash receipts. (AS 2201.42 and .44)

- The firm did not identify and test any controls over accrued rebates and other deductions. (AS 2201.39)

Issuer R – Health Care

Type of audit and related area affected

In our review, we identified deficiencies in the financial statement audit related to **Inventory**, for which the firm identified a significant risk.

Description of the deficiencies identified

The firm's substantive procedures to test the unit cost of inventory consisted of selecting a sample of items for testing. For certain items selected for testing, the firm did not perform sufficient procedures to test the unit cost because it inspected supporting documentation for only a portion of the quantity of these items held at year end. (AS 2301.08)

The firm used information produced by the issuer in its substantive procedures to test the reserve for excess and obsolete inventory. The firm did not perform any procedures to test, or test controls over, the accuracy and/or completeness of certain of this information. (AS 1105.10)

Issuer S – SPACs

Type of audit and related area affected

In our review, we identified deficiencies in the financial statement audit related to **Warrants**.

Description of the deficiencies identified

The issuer issued warrants that were recorded as liabilities. For certain of these warrants, the following deficiencies were identified:

- The firm did not perform any procedures to evaluate the reasonableness of a significant assumption the issuer used to value these warrants at year end. (AS 2501.16)

- The firm did not perform any substantive procedures to evaluate the appropriateness of the issuer's categorization of these warrants within the fair value hierarchy as set forth in FASB ASC Topic 820. (AS 2301.08)

Issuer T – Consumer Discretionary

Type of audit and related area affected

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

Description of the deficiencies identified

The firm selected for testing the issuer's cycle-count control over inventory at certain locations. The firm did not test the aspect of this control that addressed whether all inventory items at these locations were counted during the period. (AS 2201.42 and .44) In addition, the firm did not identify and test any controls that addressed the completeness of certain reports used in the operation of this control. (AS 2201.39)

Audits with a Single Deficiency

Issuer U – Real Estate

Type of audit and related area affected

In our review, we identified a deficiency in the financial statement audit related to **Long-Lived Assets**, for which the firm identified a significant risk.

Description of the deficiency identified

The issuer evaluated certain long-lived assets for possible impairment using significant assumptions it developed based on its planned course of action. The firm's approach for substantively testing the issuer's impairment assessment was to test the issuer's process, and the firm used an auditor-employed specialist to evaluate one of these assumptions. The firm did not identify that the work of the auditor-employed specialist did not provide sufficient appropriate audit evidence because it did not evaluate a significant difference between this assumption and the issuer's recent experience. Further, when evaluating the issuer's ability to carry out its planned course of action, the firm performed a sensitivity analysis for this assumption but did not evaluate the significant differences between the alternative assumptions it used in this analysis and the issuer's recent experience. (AS 1201.C6 and .C7; AS 2501.16)

Issuer V – Consumer Discretionary

Type of audit and related area affected

In our review, we identified a deficiency in the financial statement audit related to **Journal Entries**, for which the firm identified a fraud risk.

Description of the deficiency identified

To identify and select journal entries for testing, the firm identified fraud characteristics and obtained a list of all journal entries with these characteristics. The firm did not perform sufficient procedures to test those journal entries because it examined the underlying support for only certain journal entries, without having an appropriate rationale for limiting its testing to those certain journal entries. (AS 2401.61)

Issuer W – Information Technology

Type of audit and related area affected

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

Description of the deficiency identified

The firm did not perform procedures to evaluate certain indicators of potential impairment that existed at year end. (AS 2301.08)

Issuer X – Health Care

Type of audit and related area affected

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

Description of the deficiency identified

The firm did not perform any procedures to test, or test controls over, the accuracy of certain information produced by the issuer that the firm used in its substantive testing of the reserve for excess and obsolete inventory. (AS 1105.10)

Issuer Y – Consumer Discretionary

Type of audit and related area affected

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

Description of the deficiency identified

For one type of revenue at one business unit, the firm did not identify and test any controls over the accuracy of certain order information from the issuer's customer ordering system that the issuer used to record revenue. (AS 2201.39)

PART I.B: OTHER INSTANCES OF NON-COMPLIANCE WITH PCAOB STANDARDS OR RULES

This section of our report discusses certain deficiencies that relate to instances of non-compliance with PCAOB standards or rules other than those where the firm had not obtained sufficient appropriate audit evidence to support its opinion(s). This section does not discuss instances of potential non-compliance with SEC rules or instances of non-compliance with PCAOB rules related to maintaining independence.

When we review an audit, we do not review every aspect of the audit. As a result, the areas below were not necessarily reviewed on every audit. In some cases, we assess the firm's compliance with specific PCAOB standards or rules on other audits that were not reviewed and include any instances of non-compliance below.

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

- In one of 25 audits reviewed, the firm, when testing journal entries for evidence of possible material misstatement due to fraud, did not perform sufficient procedures to determine whether the journal entry population from which it made its selections was complete. In this instance, the firm was non-compliant with AS 1105, *Audit Evidence*.
- In one of 29 audits reviewed, the firm did not include all relevant work papers in the final set of audit documentation it was required to assemble. In this instance, the firm was non-compliant with AS 1215, *Audit Documentation*.
- In one of 29 audits reviewed, an other auditor used by the firm had obtained a letter of representation from management for one of the issuer's non-U.S. components, but the firm did not retain this letter. In this instance, the firm was non-compliant with AS 1215, *Audit Documentation*.
- In two of 19 audits reviewed, the firm did not make certain required communications to the audit committee related to the name, location, and planned responsibilities of other accounting firms that performed audit procedures in the audit. In these instances, the firm was non-compliant with AS 1301, *Communications with Audit Committees*.
- In one of 29 audits reviewed, the firm did not evaluate certain factors when determining that there were no risks of material misstatement related to a relevant assertion for a significant account and disclosure. In this instance, the firm was non-compliant with AS 2110, *Identifying and Assessing Risks of Material Misstatement*.
- In one of 19 audits reviewed, the firm did not include in its report on ICFR a disclosure regarding the exclusion of acquired businesses from the scope of both management's assessment and the firm's audit of ICFR. In this instance, the firm was non-compliant with AS 2201*, An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- In 12 of 25 audits reviewed, the firm, when testing journal entries for evidence of possible material misstatement due to fraud, did not have an appropriate rationale for limiting its testing

of entries it identified as having certain fraud risk characteristics to certain entries. In these instances, the firm was non-compliant with AS 2401, *Consideration of Fraud in a Financial Statement Audit*.

- In six of 25 audits reviewed, the firm, when testing journal entries for evidence of possible material misstatement due to fraud, did not appropriately consider the characteristics of potentially fraudulent journal entries in determining the criteria it used to identify and select journal entries for testing. In these instances, the firm was non-compliant with AS 2401, *Consideration of Fraud in a Financial Statement Audit*.
- In three of 15 audits reviewed, the firm did not make a required communication to management related to one or more identified misstatements. In these instances, the firm was non-compliant with AS 2810, *Evaluating Audit Results*.
- In three of 23 audits reviewed, the firm's communication of a critical audit matter in the audit report included language that was inconsistent with information in the firm's audit documentation. In these instances, the firm was non-compliant with AS 3101, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion.*
- In one of 19 audits reviewed, the firm's report on Form AP omitted information related to the participation in the audit by other accounting firms. In this instance, the firm was non-compliant with PCAOB Rule 3211, *Auditor Reporting of Certain Audit Participants*.

PART I.C: INDEPENDENCE

This section of our report discusses instances of potential non-compliance with SEC rules or instances of non-compliance with PCAOB rules related to maintaining independence. An instance of potential non-compliance with SEC rules or an instance of non-compliance with PCAOB rules does not necessarily mean that the Board has concluded the firm was not objective and impartial throughout the audit and professional engagement period. Although this section includes instances of potential non-compliance that we identified and the firm brought to our attention, there may be other instances of non-compliance with SEC or PCAOB rules related to independence that were not identified through our procedures or the firm's monitoring activities.

PCAOB-Identified

We identified the following instances of potential non-compliance with SEC rules or instances of non-compliance with PCAOB rules related to maintaining independence:

Under Rule 2-01(c)(7) of Regulation S-X, an accountant is not independent if it does not obtain audit committee pre-approval for audit and non-audit services. In 20 audits reviewed, we identified five instances for one issuer in which this circumstance appears to have occurred related to certain non-audit services.

Firm-Identified

During the inspection, the firm brought to our attention that it had identified, through its independence monitoring activities for a nine-month period, one instance for one issuer,[2] representing less than 1% of the firm's total reported issuer audits, in which the firm appeared to have impaired its independence because it may not have complied with Rule 2-01(b) of Regulation S-X related to maintaining independence. This instance of potential non-compliance did not involve non-U.S. associated firms.

While we have not evaluated the underlying reasons for the instance of potential non-compliance, the number, large or small, of firm-identified instances of potential non-compliance may be reflective of the size of the firm, including the number of non-U.S. associated firms in the global network; the design and effectiveness of the firm's independence monitoring activities; and the size and/or complexity of the issuers it audits, including the number of affiliates of the issuer. Therefore, we caution against making any comparison of firm-identified instances of potential non-compliance across firms.

The firm reported one instance of potential non-compliance regarding an indemnification clause that appears to be inconsistent with the general standard of independence set out in Rule 2-01(b) of Regulation S-X. This instance related to the firm including a clause in its engagement letter with an issuer audit client that may have resulted in the audit client agreeing to indemnify the firm with respect to certain liabilities for this audit.

The firm has reported to us that it has evaluated this instance of potential non-compliance and determined that its objectivity and impartiality were not impaired. The firm also reported to us that it has communicated this instance to the issuer's audit committee as required by PCAOB Rule 3526.

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[2] The firm-identified instance of potential non-compliance does not necessarily relate to the issuer audits that we selected for review.

PART II: OBSERVATIONS RELATED TO QUALITY CONTROL

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

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

This report does not reflect changes or improvements to the firm's system of quality control that the firm may have made subsequent to the period covered by our inspection. The Board does consider such changes or improvements in assessing whether the firm has satisfactorily addressed the quality control criticisms or defects no later than 12 months after the issuance of this report.

When we issue our reports, we do not make public criticisms of, and potential defects in, the firm's system of quality control, to the extent any are identified. If a firm does not address to the Board's satisfaction any criticism of, or potential defect in, the firm's system of quality control within 12 months after the issuance of our report, we will make public any such deficiency.

APPENDIX A: FIRM’S RESPONSE TO THE DRAFT INSPECTION REPORT

Pursuant to Section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(a), the firm provided a written response to a draft of this report. Pursuant to Section 104(f) of the Act and PCAOB Rule 4007(b), the firm’s response, excluding any portion granted confidential treatment, is attached hereto and made part of this final inspection report.

The Board does not make public any of a firm’s comments that address a nonpublic portion of the report unless a firm specifically requests otherwise. In some cases, the result may be that none of a firm’s response is made publicly available.

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

Tel: 212-885-8000
Fax: 212-697-1299
www.bdo.com

100 Park Avenue
New York, NY 10017

April 15, 2024

Ms. Christine Gunia
Director
Division of Registration and Inspections
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, DC 20006

Re: Response to Part I of the Draft Report on the 2023 Inspection of BDO USA, P.C.

Dear Ms. Gunia:

On behalf of BDO USA, P.C., we are pleased to provide our response to Part I of the Public Company Accounting Oversight Board's ("PCAOB" or the "Board") Draft Report on the 2023 Inspection of BDO USA, P.C. The Board's inspection process plays an integral role in enhancing audit quality. We continue to support the PCAOB's mission of protecting investors and furthering the public interest in the preparation of informative, accurate, and independent audit reports.

We have evaluated each of the matters described in Part I of the Draft Report and have taken appropriate actions in accordance with PCAOB standards, AS 2901, *Consideration of Omitted Procedures After the Report Date*, and where applicable, AS 2905, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report.*

We recognize the important role we play in protecting the interest of investors and the integrity of the capital markets and are therefore steadfast in our commitment to audit quality as our highest priority. We detail the numerous investments we are making to improve the quality of our audits at: https://www.bdo.com/insights/assurance/bdo-usa-audit-quality-journey

The PCAOB's inspection process, including dialogue with the staff, assists us in improving our audit performance, our underlying quality control system, and ultimately the reliability of financial reporting. We look forward to continuing our dialogue with the PCAOB and its staff and would be happy to address any questions you may have.

Sincerely,

Wayne Berson
CEO

William Eisig
Assurance National Managing Principal