PCAOB
Public Company Accounting Oversight Board

1666 K Street, N.W.
Washington, DC 20006
Telephone: (202) 207-9100
Facsimile: (202) 862-8433
www.pcaobus.org

Report on

2012 Inspection of PricewaterhouseCoopers LLP
(Headquartered in New York, New York)

Issued by the

Public Company Accounting Oversight Board

August 20, 2013

THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT

PORTIONS OF THE COMPLETE REPORT ARE OMITTED FROM THIS DOCUMENT IN ORDER TO COMPLY WITH SECTIONS 104(g)(2) AND 105(b)(5)(A) OF THE SARBANES-OXLEY ACT OF 2002

PCAOB RELEASE NO. 104-2013-148

PCAOB Release No. 104-2013-148

Public Company Accounting Oversight Board

2012 INSPECTION OF PRICEWATERHOUSECOOPERS LLP

Preface

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

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

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

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

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

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

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's staff ("the inspection team") conducted primary procedures for the inspection from November 2011 to February 2013. The inspection team performed field work at the Firm's National Office and at 29 of its approximately 66 U.S. practice offices.

A. Review of Audit Engagements

The 2012 inspection of the Firm included reviews of aspects of 52 audits performed by the Firm and reviews of the Firm's audit work on two other issuer audit engagements in which the Firm played a role but was not the principal auditor. The inspection team identified matters that it considered to be deficiencies in the performance of the work it reviewed. One of the deficiencies relates to auditing aspects of an issuer's financial statements that the issuer restated after the primary inspection procedures.[3/] In addition, for one of the audits described below, the Firm revised its opinion on the effectiveness of the issuer's internal control over financial reporting ("ICFR") to express an adverse opinion.

The inspection team considered certain of the deficiencies that it observed to be audit failures. As used in PCAOB inspection reports, the term "audit failure" refers to a circumstance where the inspection team identified one or more deficiencies in an audit that were of such significance that it appeared that the Firm, at the time it issued its audit report, had failed to obtain sufficient appropriate audit evidence to support its audit

---

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

opinion on the financial statements and/or on the effectiveness of ICFR. The audit deficiencies that reached this level of significance are described below.[4/]

A.1. Issuer A

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

- The Firm's procedures related to revenue and deferred revenue were insufficient. Specifically –

  - The issuer's process for recording revenue transactions and deferred revenue involved several information technology systems and multiple transfers of data between these various systems. The Firm failed to identify and test any controls over the accuracy and completeness of several of these data transfers. In addition, the Firm tested a control consisting of the review of data transferred between two of these systems, but the Firm's procedures were insufficient, as it limited its testing to determining that the review had occurred, without evaluating whether the control operated at a level of precision that would prevent or detect material misstatements.

  - The Firm concluded that certain system-generated reports used in the operation of controls were accurate and complete based on testing performed in a prior year's audit ("benchmarking"). The Firm, however, failed to obtain assurance that the relevant underlying programs of two applications and the parameters used to generate the relevant reports had not changed since the reports

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

generated by those systems had last been tested, as the Firm's procedures to test access to programs and program changes were insufficient. Specifically, the Firm failed to determine whether users could make unauthorized changes to the revenue recognition rules or rates within one of the applications and failed to evaluate certain program changes made to both applications.

- o The Firm's planned approach for auditing revenue included performing substantive analytical procedures, testing revenue cut-off, and recalculating deferred revenue. The Firm failed to test the accuracy and completeness of certain data and reports it used in each of these tests.

- The Firm's procedures related to the issuer's current and deferred income taxes were insufficient. Specifically –

  - o The Firm selected for testing certain review controls over the current and deferred income taxes; however, it failed to sufficiently test these controls. Specifically, the Firm's procedures were limited to obtaining evidence that such reviews had occurred, comparing information used in the controls to supporting documentation or data, and inquiring of management. The Firm's procedures did not include evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements.

  - o The issuer asserted that earnings from foreign subsidiaries were permanently reinvested outside of the U.S., and it did not record a deferred tax liability for such earnings. The Firm failed to identify and test any controls regarding the issuer's determination that the earnings were permanently reinvested.

  - o The issuer claimed certain tax benefits that were dependent upon the issuer meeting certain criteria. The Firm failed to identify and test any controls over the issuer's determination that it qualified for these tax incentives. In addition, the Firm failed to test the accuracy and completeness of the data the Firm used in its testing to determine whether the issuer was meeting the criteria to qualify for the tax incentives.

- The issuer acquired a business during the year and disclosed that the allocation of the purchase price to the assets acquired was preliminary as of its year end. The Firm's procedures to evaluate the reasonableness of the forecasts the issuer used to determine the preliminary values of acquired intangible assets ("valuation forecasts") were insufficient. Specifically, the Firm's procedures included comparing the valuation forecasts to the forecasts the issuer used in its annual goodwill impairment test; the Firm, however, failed to evaluate significant differences between the two forecasts, beyond inquiring of management. Further, the Firm failed to consider whether the significant differences between the actual results for the year under audit and the projected results for that year that were included in the valuation forecasts had implications related to the reasonableness of the valuation forecasts.

- The Firm selected for testing certain review controls over the accounting for business combinations; however, it failed to sufficiently test these controls. Specifically, the Firm's procedures were limited to obtaining evidence that such reviews had occurred, comparing information in certain documents used in the operation of the controls to supporting documents, and reading memoranda and other documents prepared as a part of the controls. In addition, the Firm referenced its substantive testing when addressing its evaluation of the effectiveness of these controls; however, the Firm failed to test, through any of its procedures, whether the controls operated at a level of precision that would prevent or detect material misstatements related to the accounting for business combinations.

A.2. Issuer B

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

- The Firm failed to identify and test any controls over the completeness of a significant type of sales incentive recorded as a reduction of revenue. In addition, for a significant subset of these incentives, the Firm failed to identify and test any controls over the timing of the recognition, and in some cases the amount, of the sales incentives.

- The Firm's procedures to test the issuer's controls over accounting for income taxes were insufficient. Specifically –

    - o The Firm's procedures to test certain review controls were limited to obtaining evidence that the reviews had occurred and testing the mathematical accuracy of certain supporting documents, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements.

    - o The issuer asserted that earnings from certain of its foreign subsidiaries were permanently reinvested outside of the U.S. and therefore did not include those earnings in its calculation of its deferred tax liabilities. There was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had tested any controls over the issuer's evaluation of evidence that supported this assertion.

- The issuer established a tax structure designed to allow for the repatriation of cash from certain of its foreign subsidiaries to occur on a tax-free basis. The Firm, however, failed to perform sufficient procedures to evaluate the issuer's assertion that cash it repatriated under this structure during the year was not subject to U.S. taxes. Specifically, the Firm limited its procedures to inquiring of management and reading a memorandum prepared by management. Further, it failed to examine any of the agreements associated with, or test the completeness of, the repatriations.

- The Firm failed to perform sufficient substantive procedures related to the issuer's provision for income taxes and its reserve for uncertain tax positions. Specifically, the Firm selected for testing certain items that the issuer recorded in its provision for income taxes and its liability for uncertain tax positions, but the Firm failed to perform sufficient procedures to test these items. Specifically, for certain of these items, the Firm failed to (a) test the accuracy and completeness of the underlying data the issuer used to develop the amount recorded, (b) evaluate the reasonableness of the significant assumptions used to develop the amount recorded, and/or (c) obtain corroboration of management's explanation as to why there had been no change in the amount recorded for the uncertain tax position since the prior year.

A.3. Issuer C

In this audit, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinion on the financial statements. Specifically –

- To test the value of certain available-for-sale securities ("mortgage-backed securities"), the Firm sought to obtain prices from outside pricing vendors. The Firm received such prices for only a small number of the mortgage-backed securities. For the remainder, the Firm obtained certain data related to the mortgage-backed securities, and determined that it expected the value of the majority of the mortgage-backed securities to fall within a specified range. The Firm tested the value of a small number of the mortgage-backed securities that fell outside this range, as well as three other mortgage-backed securities that met certain collateral-performance criteria. The Firm used the results of this testing to conclude on the entire population of mortgage-backed securities for which no price was obtained from an outside pricing vendor. The Firm's testing approach for the mortgage-backed securities was insufficient. Specifically –
  - The Firm developed its expected range of values for the mortgage-backed securities without correlating the data to the range.
  - The Firm failed to perform sufficient procedures with respect to the values of mortgage-backed securities outside of its expected range of values. Specifically, the Firm's selection of mortgage-backed securities that fell outside its expected range was not designed to be representative of that population of mortgage-backed securities, and the Firm failed to perform procedures to test a significant number of the mortgage-backed securities that fell outside this range.
- To test the value of another type of available-for-sale debt securities ("private placements"), the Firm developed an independent estimate based on the unadjusted prices for publicly traded bonds that were

purportedly comparable based on the issuer, ratings, coupon rates, and maturities. The Firm's testing approach for the private placements was deficient. Specifically –

- The Firm failed to perform sufficient procedures to evaluate whether the private placements were comparable to the publicly traded bonds, as it did not consider whether the private placements had features that were different from the publicly traded bonds.

- The Firm established a range of reasonable prices for each private placement, using the minimum and maximum prices of publicly traded bonds that it deemed to be comparable. In some cases, this range was not sufficiently precise for determining the reasonableness of the private placements' values and the Firm did not perform additional procedures to identify expected prices for those private placements. For certain private placements that fell outside of the range, the Firm compared the issuer's price to a price provided by an external party. There was no evidence in the audit documentation, and no persuasive other evidence, however, that the Firm had obtained an understanding of the specific methods and assumptions underlying the fair value measurements that it obtained from the external party.

- To test the fair value of certain derivatives, the Firm developed independent estimates and compared those estimates to the recorded fair values. This testing was deficient in the following respects –

  - The Firm established thresholds for investigation of differences, but those thresholds were not designed so that they would reasonably be expected to detect material misstatements in the recorded derivatives balance.

  - The Firm failed to sufficiently evaluate the differences for individual derivatives that were in excess of its thresholds. Specifically, the Firm's analyses of certain of these differences were limited to general observations about certain characteristics of the derivatives.

A.4. Issuer D

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

- The Firm failed to sufficiently test controls over the valuation of fixed-maturity investment securities. Specifically, the majority of the controls the Firm tested used data and reports that were subject to automated application controls. The Firm planned to use a benchmarking strategy to test these automated application controls, but it failed to appropriately execute that strategy, as its procedures to verify that the automated application controls had not changed since they were last tested were limited to inquiries of management. In addition, other controls that the Firm tested over the valuation of investment securities used data and reports that were not subject to the automated application controls, and the Firm failed to identify and test any controls over these data and reports.

- The Firm's testing of the valuation of two categories of financial instruments, which represented a significant portion of the issuer's portfolio, was insufficient. Specifically, the Firm's primary procedures were to test the fair value of individual financial instruments that met certain criteria, as well as an additional three to five financial instruments from each category, but these procedures were not designed to enable the Firm to support a conclusion on the valuation of the remaining financial instruments in those categories. The Firm performed no procedures regarding the remaining population in one of the two categories of financial instruments. For the other category, the Firm performed certain procedures related to the remaining population, but this testing was insufficient as (a) the Firm tested only inputs to the issuer's valuation model without evaluating the appropriateness of the model itself, and (b) the Firm's comparison of actual sale prices during the year to previously recorded prices for certain investments revealed differences over the Firm's threshold that the Firm investigated only through inquiry.

A.5. Issuer E

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

- The Firm's procedures to test the issuer's accounting for a number of business combinations completed during the year were insufficient. Specifically –
  - The Firm failed to test the accuracy and completeness of the acquiree's historical data used in determining the fair value of a significant portion of the acquired intangible assets and property and equipment.
  - The Firm failed to evaluate the reasonableness of certain significant assumptions used in determining the fair values of the acquired assets, beyond inquiry of management and, for one acquisition, also inquiry of the issuer's specialist.
  - The Firm's procedures to evaluate one assumption, the discount rate, were limited to inquiry and a comparison of the discount rate used in certain acquisitions to the weighted average cost of capital used in the issuer's prior-year goodwill impairment analysis.
- The issuer's process for recognizing the majority of revenue from one significant customer was different from the revenue process for its other customers. The Firm failed to identify and test any controls over the occurrence of revenue from the significant customer.

A.6. Issuer F

In this audit, the Firm failed to sufficiently test controls over (a) the issuer's accounting for business combinations and (b) the disposition of businesses and the reporting of discontinued operations. Specifically, the Firm selected for testing certain review controls that were part of the issuer's period-end financial reporting process, but its testing was limited to obtaining evidence that reviews had occurred, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements related to these areas, and without determining whether these controls addressed the accounting requirements for discontinued operations.

A.7 Issuer G

In this audit, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and on the effectiveness of ICFR. The issuer calculated the value of its inventory using the retail inventory method of accounting ("the cost calculation"). The Firm's testing related to the valuation of inventory was deficient as follows –

- The Firm failed to perform sufficient procedures to test the issuer's markdowns of the retail price of inventory, which were important inputs in the cost calculation. While the Firm tested a selection of sales transactions of marked-down inventory during the year, the Firm failed to test whether all approved markdowns were recorded in the issuer's records and whether the markdowns recorded at year end were accurate.

- The Firm selected for testing a control over markdowns, but it failed to test the attribute of the control that addressed whether approved markdowns were entered into the issuer's system.

- The Firm selected for testing a review control over the cost calculation; however, it failed to evaluate whether the control was designed to operate at a level of precision that would prevent or detect material misstatements.

A.8. Issuer H

In this audit, the Firm failed to identify that the issuer had incorrectly calculated the amount of the goodwill impairment it recorded during the year. The Firm also failed to identify and evaluate, as a potential material weakness, a control deficiency related to the issuer's goodwill impairment process.

A.9. Issuer I

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

- The Firm's tests of controls over two significant categories of revenue were insufficient. Specifically –
  - The Firm selected for testing certain review controls over these categories of revenue; however, it failed to sufficiently test these controls. Specifically, the Firm's procedures were limited to obtaining evidence that such reviews had occurred and confirming that certain variances were explained, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements.
  - The Firm failed to identify and test any controls over the completeness of system-generated reports the issuer used in the operation of certain manual controls over one of these categories of revenue.
- The Firm's tests of controls over the accounting for property, plant, and equipment were insufficient. Specifically –
  - The Firm failed to sufficiently test certain review controls that it selected. Specifically, for one control, the Firm's procedures were limited to obtaining evidence that the review had occurred, without evaluating whether the control operated at a level of precision that would prevent or detect material misstatements. For another control, the Firm used the results of its substantive procedures to update its control testing from the date of its interim testing to the year end, but those procedures did not directly test the control.
  - For a portion of the year, management used an external party to perform certain controls. During the year, the issuer terminated the agreement with the external party and began to perform certain of these controls on its own.

- The Firm failed to sufficiently test two of these controls after the termination of the agreement. Specifically, for one control, the Firm limited its procedures to inquiry of the issuer's internal audit group. For a second control, the Firm stated that its substantive procedures provided evidence of the effectiveness of the control after the termination of the agreement, but those procedures did not directly test the control, other than by confirming that certain actions that constituted a part of the control had occurred.

- The Firm failed to identify and test any controls operating after the termination of the agreement that addressed the reasonableness of the rates the issuer used to capitalize certain indirect costs to property, plant, and equipment.

A.10. Issuer J

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

- The Firm performed a dual-purpose test of the issuer's physical inventory cycle counts at a sample of warehouses controlled by external parties. The Firm's procedures were insufficient, as it (a) failed to identify and test any controls over the reports used by the external parties and the issuer as part of the cycle-count control, and (b) limited its testing of daily cycle counts to observing only one cycle count at each of two locations.

- The Firm observed full physical inventory counts at a sample of the issuer's retail locations, but failed to test controls over the recording of the results of the counts in the inventory sub-ledger. Further, the Firm identified differences between its counts and the issuer's counts at certain locations, but failed to (a) obtain an understanding of the reasons for the differences, (b) obtain further evidence to conclude on the existence and completeness of the inventory, and (c) evaluate whether the count differences indicated a control deficiency.

- The Firm selected for testing three review controls over the issuer's accounting for its in-transit inventory, but its tests of these controls were insufficient. Specifically, for one of the controls, the Firm's testing was limited to obtaining evidence that the reports used in the performance of the control were prepared and distributed, without testing whether the reports had been reviewed pursuant to the control's requirements. For the other two controls, the Firm's testing was limited to obtaining evidence that reviews had occurred. For all three controls, the Firm's procedures did not include determining the nature of the reviews and evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements.

- The Firm used the work of the issuer's internal audit group as evidence of the valuation, existence, and completeness of a significant component of the issuer's in-transit inventory, but it failed to obtain an understanding of the nature, timing, and extent of the procedures performed by internal audit and failed to test internal audit's work.

A.11. Issuer K

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

- For certain of the issuer's locations that in the aggregate presented a reasonable possibility of material misstatement, the Firm failed to perform substantive procedures to test revenue, accounts receivable, and inventory.

- The issuer calculated its liability for the standard warranty that it offered for each product ("base warranty reserves") using a separate spreadsheet for each product. The Firm failed to sufficiently test the issuer's base warranty reserves and the related controls. Specifically –

  - The Firm selected for testing certain review controls over the determination of the base warranty reserves. The Firm, however, failed to sufficiently test these controls, because its procedures were limited to obtaining evidence that such reviews had occurred and determining that certain variances were investigated, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements related to the base warranty reserves.

- The Firm failed to evaluate the reasonableness of significant assumptions management used to determine the base warranty reserves.

- The Firm failed to test the completeness of the data the issuer used to develop its base warranty reserves.

- The Firm failed to sufficiently test the formulas in the spreadsheets used to calculate the base warranty reserves, as it limited its testing to recalculating the base warranty reserve for only one product, even though the issuer used multiple manually prepared spreadsheets.

- The Firm failed to perform sufficient testing of deferred revenue related to extended warranty contracts and of the reserve for loss contracts related to extended warranties. Specifically –

  - The Firm selected for testing certain review controls over the accounting for extended warranty contracts, but its testing of these controls was insufficient. Specifically, the Firm limited its procedures to obtaining evidence that such reviews had occurred and inquiring of management, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements related to extended warranty contracts.

  - The Firm failed to perform sufficient substantive procedures to test deferred revenue from extended warranty contracts. Specifically, the Firm tested deferred revenue at an interim date, but it failed to perform procedures to extend its conclusions to the year end. Further, the Firm failed to perform procedures to test the reserve for loss contracts.

A.12. Issuer L

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

- The Firm's substantive testing of the issuer's investment securities was insufficient, because the Firm confirmed the existence of these securities with the issuer's investment manager, but not with the custodian. In addition, the Firm failed to identify and test any controls over the existence of the investment securities.

- The Firm selected for testing two review controls over the issuer's determination of its liability for uncertain tax positions, but its testing of these controls was insufficient. Specifically, the Firm failed to evaluate whether the controls operated at a level of precision that would prevent or detect material misstatements, as the Firm's testing was limited to observing evidence that the reviews had occurred.

- The Firm failed to perform sufficient procedures related to the issuer's accounting for foreign income taxes. Specifically –

    - The Firm failed to sufficiently test controls over the issuer's accounting for foreign income taxes. Specifically, the Firm's procedures were limited to (a) observing evidence that the reviews or activities that constituted a part of the operation of the control had occurred, and (b) in some instances, comparing certain documents used in the control to supporting documentation. The Firm's procedures to test these controls did not include evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements.

    - The Firm failed to perform sufficient procedures to test the components of the provision for foreign income taxes. For the issuer's foreign locations that the Firm selected for testing, the Firm (a) recalculated the income tax expense for each location (based on pre-tax income and the applicable statutory rate) and compared the recalculated amount to the recorded amount, and (b) tested certain tax payments and refunds. When comparing the recalculated amount to the recorded amount, the Firm did not investigate certain significant differences, and did not obtain corroboration of management's explanations of other significant differences. Further, the Firm failed to test the completeness of the foreign deferred tax assets and liabilities.

- The Firm identified audit adjustments related to the issuer's income taxes, as well as an unsupported liability for an uncertain tax position, but the Firm failed to evaluate whether the adjustments and the unsupported liability were, either individually or in the aggregate, indicators of potential material weaknesses in the issuer's internal control.

A.13. Issuer M

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

- The Firm selected a control for testing that consisted of the involvement of the issuer's executives in reviewing non-standard transactions. The Firm asserted that this control covered the accounting for business combinations and, for two of the issuer's significant business units, the review of customer contracts for the evaluation of unusual terms and conditions related to the accounting for revenue. The Firm's testing of this control was insufficient, as it limited its testing to inquiring of management. In addition, the Firm referenced its substantive testing when addressing its evaluation of the effectiveness of this control with respect to the accounting for business combinations. The Firm, however, failed to test, through any of its procedures, whether the control operated at a level of precision that would prevent or detect material misstatements related to these areas.

- The Firm's testing of other controls over one of the significant categories of revenue for one of these business units was also insufficient. Specifically, the Firm failed to test any controls over the accuracy and completeness of system-generated data and reports that the issuer used in the performance of certain of these controls. In addition, for certain review controls over this revenue, the Firm's testing was limited to obtaining evidence that such reviews had occurred, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements.

A.14. Issuer N

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

- During the year, the issuer completed the acquisition of a significant business. The Firm's testing related to the accounting for business combinations was deficient in the following respects –

  - The Firm failed to sufficiently test a control consisting of the review of the issuer's accounting research memoranda and related journal entries, which was a period-end financial reporting process control that the Firm identified as addressing the risks associated with the accounting for business combinations. Specifically, the Firm's procedures were limited to determining that a review had occurred. In addition, the Firm referenced its substantive testing when addressing its evaluation of the effectiveness of this control. The Firm, however, failed to test, through any of its procedures, whether the control operated at a level of precision that would prevent or detect material misstatements related to business combinations.

  - The issuer used two external valuation specialists to determine the fair value of the acquired property and equipment. The Firm failed to test certain underlying data used by one of the valuation specialists. In addition, the Firm failed to evaluate the appropriateness of the methodology and the reasonableness of the assumptions the other specialist used.

  - Before the business combination, the issuer had owned an interest in the acquired entity that it accounted for under the equity method. In accounting for the business combination, the issuer adjusted the recorded value of this interest to fair value. When testing the fair value, the Firm failed to take into account the work of the issuer's external valuation specialists, which suggested different fair values from those recorded by the issuer.

- The Firm's procedures related to the issuer's accounting for income taxes were insufficient. Specifically –
    - The Firm's testing of the issuer's control related to uncertain tax positions was insufficient, as the Firm failed to evaluate whether this control operated at a level of precision that would prevent or detect material misstatements.
    - The Firm's procedures to substantively test certain liabilities for uncertain tax positions were insufficient. Specifically –
        - For certain of these positions, the Firm failed to evaluate the reasonableness of the percentages that management applied to the individual positions to determine the liability.
        - For certain other positions, the Firm limited its testing to verifying that the amounts were the same as those recorded in the prior year, without evaluating the reasonableness of assumptions that management used to determine the liability, including the assumption that the amounts should be the same as those in the prior year.
        - For another position, the Firm failed to test the issuer's recording of a significant reduction in the liability for the position.

A.15. Issuer O

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

- The Firm failed to test any controls that would address whether the issuer's allocation of overhead costs to inventory was appropriate. In addition, the Firm failed to perform substantive procedures to test the overhead costs allocated to inventory during the year, other than comparing the costs to a schedule that it obtained from the issuer but did not test.

- The issuer reported its convertible debt securities at amortized cost on its balance sheet and disclosed the fair value of these securities in the notes to the financial statements. To test the fair value of these securities, the Firm obtained prices from three pricing services. The Firm, however, failed to obtain an understanding of the specific methods and assumptions underlying the fair value measurements that it obtained from the pricing services.

A.16. Issuer P

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

- The Firm selected two review controls over the issuer's accounting for its liability for uncertain tax positions, but its tests of these controls were insufficient. Specifically, the Firm's testing was limited to obtaining evidence that such reviews had occurred. In addition, the Firm referenced its substantive testing when addressing its evaluation of the effectiveness of one of the controls. The Firm, however, failed to test, through any of its procedures, whether the controls operated at a level of precision that would prevent or detect material misstatements related to this process.

- The Firm's substantive procedures to test the issuer's liability for uncertain tax positions were insufficient. Specifically, the Firm chose to review and test management's process for developing these estimates, but it failed to test certain significant inputs, and to evaluate the appropriateness of the methodology and the reasonableness of the assumptions, that the issuer used to determine certain components of the liability.

A.17. Issuer Q

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

- The issuer recognized a significant portion of its revenue under the percentage-of-completion method of accounting. The Firm selected for testing certain review controls over contract costs incurred to date and over estimated costs to complete contracts, which were important inputs for the percentage-of-completion calculation; however, its testing of these controls was insufficient. Specifically, the Firm's procedures were limited to attending a small number of meetings that constituted a part of certain of the reviews and observing documentary evidence that reviews had occurred, without evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements. In addition, the Firm failed to test controls over the accuracy and completeness of the data and reports the issuer used in the performance of the review controls.

- The Firm failed to test the effectiveness of any controls over the issuer's impairment evaluation for intangible assets with definite lives.

A.18. Issuer R

In this audit, the Firm failed to obtain sufficient appropriate audit evidence to support its audit opinions on the financial statements and on the effectiveness of ICFR. The Firm performed certain procedures with respect to the issuer's evaluation of the possible impairment of unproved oil and gas properties, which the issuer performed on a property-by-property basis. These procedures, however, were not sufficient, as –

- The Firm failed to test any controls over the issuer's process for periodically evaluating its unproved properties for impairment prior to the lease expiration date.

- The Firm failed to test certain data and evaluate the reasonableness of certain significant assumptions that the issuer used in its evaluation of unproved properties for impairment.

A.19. Issuer S

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

- The Firm's procedures to test controls over the timing of revenue recognition and the recording of related accounts receivable were insufficient. Specifically, the Firm selected for testing certain review controls over the issuer's invoicing and shipping processes, but failed to test several important attributes of those controls.

- The Firm's planned approach to auditing revenue included the performance of substantive analytical procedures. The Firm's analytical procedures, however, provided little to no substantive assurance, because –

    - The Firm developed its expectations based on the issuer's budget, adjusted for historical performance or industry trends, without a rationale as to why these amounts could be expected to be predictive of the issuer's current-period revenue.

    - The Firm discussed with management the unexpected differences that were greater than its established threshold. The Firm failed to obtain corroboration of management's explanations, beyond reading certain issuer-prepared reports that it did not test. In addition, remaining differences were greater than the Firm's established threshold. The Firm, however, failed to investigate those differences or evaluate whether the differences represented misstatements.

A.20. Issuer T

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

- The Firm's testing of a review control over the issuer's valuation of inventory was insufficient. Specifically, the Firm's testing was limited to determining that the review had occurred, without evaluating whether the control operated at a level of precision that would prevent or detect material misstatements. In addition, the issuer used certain system-generated data and reports as part of the operation of the review control; the Firm, however, failed to test controls over the accuracy and completeness of the data and reports.

- The Firm failed to test certain important inputs and failed to assess the reasonableness of certain significant assumptions the issuer used to determine the value of the inventory.

A.21. Issuer U

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

- The Firm selected for testing three controls over current and deferred income taxes, but it failed to sufficiently test these controls. Specifically, for two review controls, the Firm's testing was limited to observing evidence that the reviews had occurred. For a reconciliation control, the Firm's testing was limited to determining whether the preparer of the reconciliation was the person the control description specified. The Firm's procedures to test these controls did not include evaluating whether the controls operated at a level of precision that would prevent or detect material misstatements.

- The Firm's substantive procedures to test the issuer's accounting for income taxes were insufficient. Specifically, the Firm failed to evaluate the appropriateness of the methodology and the reasonableness of significant assumptions, and/or test certain important data, that the issuer used to calculate certain deferred tax assets and liabilities, components of the provision for income tax expense (including certain tax credits), and the issuer's liability for uncertain tax positions.

B. Auditing Standards

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

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

AS No. 13 requires the auditor to design and implement audit responses that address the identified risks of material misstatement, and AS No. 15, *Audit Evidence* ("AS No. 15") requires the auditor to plan and perform audit procedures to obtain sufficient appropriate audit evidence to provide a reasonable basis for the audit opinion. Sufficiency is the measure of the quantity of audit evidence, and the quantity needed is affected by the risk of material misstatement and the quality of the audit evidence obtained. The appropriateness of evidence is measured by its quality; to be appropriate, evidence must be both relevant and reliable in support of the related conclusions.

AS No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* ("AS No. 5") and AS No. 13 establish requirements regarding testing and evaluating internal control over financial reporting. In an audit of internal control over financial reporting in an integrated audit, AS No. 5 requires the auditor to plan and perform the audit to obtain appropriate evidence that is sufficient to support the auditor's opinion on internal control over financial reporting as of the date of that opinion. AS No. 13 requires that, if the auditor plans to assess control risk at less than the maximum and to base the nature, timing, and extent of substantive audit procedures on that lower assessment, the auditor must obtain evidence that the controls tested were designed and operating effectively during the entire period for which the auditor plans to rely on controls to modify the substantive procedures.

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

PCAOB Auditing Standards	Issuers
PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*	A, B, D, E, F, G, I, J, K, L, M, N, O, P, Q, R, S, T, and U
AS No. 9, *Audit Planning*	K
AS No. 13, *The Auditor's Responses to the Risks of Material Misstatement*	B, G, L, M, and P
AS No. 14, *Evaluating Audit Results*	L
AS No. 15, *Audit Evidence*	A and J
AU Section 322, *The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements*	J
AU Section 326, *Evidential Matter*	O
AU Section 328, *Auditing Fair Value Measurements and Disclosures*	A, C, D, E, H, N, and O
AU Section 329, *Substantive Analytical Procedures*	A and S
AU Section 331, *Inventories*	J
AU Section 342, *Auditing Accounting Estimates*	B, G, K, L, N, P, R, T, and U

C. General Information Concerning PCAOB Inspections

Board inspections are designed to identify whether weaknesses and deficiencies exist related to how a firm conducts audits and to address any such weaknesses and deficiencies. To achieve that goal, inspections include reviews of certain aspects of selected audit work performed by the Firm and reviews of certain aspects of the Firm's quality control system. The focus on weaknesses and deficiencies necessarily carries

[5/] This table does not necessarily include reference to every auditing standard that may have been implicated by the deficiencies included in Part I.A.

through to reports on inspections and, accordingly, Board inspection reports are not intended to serve as balanced report cards or overall rating tools. Further, the inclusion in an inspection report of certain deficiencies and potential deficiencies should not be construed as an indication that the Board has made any determination about other aspects of the firm's systems, policies, procedures, practices, or conduct not included within the report.

The inspection team selects the audits and aspects to review, and the Firm is not allowed an opportunity to limit or influence the selections. In the course of reviewing aspects of selected audits, the inspection team may identify matters that it considers to be deficiencies in the performance of the work it reviews. Those deficiencies may include failures by the Firm to identify, or to address appropriately, financial statement misstatements, including failures to comply with disclosure requirements,[6/] as well as failures by the Firm to perform, or to perform sufficiently, certain necessary audit procedures. It is not the purpose of an inspection, however, to review all of a firm's audits or to identify every respect in which a reviewed audit is deficient. Accordingly, a Board inspection report should not be understood to provide any assurance that the firm's audit work, or the relevant issuers' financial statements or reporting on internal control, are free of any deficiencies not specifically described in an inspection report.

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

[6/] When it comes to the Board's attention that an issuer's financial statements appear not to present fairly, in a material respect, the financial position, results of operations, or cash flows of the issuer in conformity with applicable accounting principles, the Board's practice is to report that information to the Securities and Exchange Commission ("SEC" or "the Commission"), which has jurisdiction to determine proper accounting in issuers' financial statements. Any description in this report of financial statement misstatements or failures to comply with SEC disclosure requirements should not be understood as an indication that the SEC has considered or made any determination regarding these issues unless otherwise expressly stated.

In some cases, the conclusion that a firm failed to perform a procedure may be based on the absence of documentation and the absence of persuasive other evidence, even if the firm claimed to have performed the procedure. AS No. 3, *Audit Documentation* ("AS No. 3") provides that, in various circumstances including PCAOB inspections, a firm that has not adequately documented that it performed a procedure, obtained evidence, or reached an appropriate conclusion must demonstrate with persuasive other evidence that it did so, and that oral assertions and explanations alone do not constitute persuasive other evidence.

Inclusion of a deficiency in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the firm's attention. When audit deficiencies are identified after the date of the audit report, PCAOB standards require a firm to take appropriate actions to assess the importance of the deficiencies to the firm's present ability to support its previously expressed audit opinions. Depending upon the circumstances, compliance with these standards may require the firm to perform additional audit procedures, or to inform a client of the need for changes to its financial statements or reporting on internal control, or to take steps to prevent reliance on previously expressed audit opinions.[7/]

In addition to evaluating the quality of the audit work performed on specific audits, the inspection included review of certain of the Firm's practices, policies, and processes related to audit quality. This review addressed practices, policies, and procedures concerning audit performance and the following five areas (1) management structure and processes, including the tone at the top; (2) practices for partner management, including allocation of partner resources and partner evaluation, compensation, admission, and disciplinary actions; (3) policies and procedures for considering and addressing the risks involved in accepting and retaining clients, including the application of the Firm's risk-rating system; (4) processes related to the Firm's use of audit work that the Firm's foreign affiliates perform on the foreign operations of the Firm's U.S. issuer audit clients; and (5) the Firm's processes for monitoring audit performance, including processes for identifying and assessing

---

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

indicators of deficiencies in audit performance, independence policies and procedures, and processes for responding to weaknesses in quality control.

END OF PART I

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

APPENDIX C

RESPONSE OF THE FIRM TO DRAFT INSPECTION REPORT

Pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(a), the Firm provided a written response to a draft of this report. Pursuant to section 104(f) of the Act and PCAOB Rule 4007(b), the Firm's response, minus any portion granted confidential treatment, is attached hereto and made part of this final inspection report.[8/]

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

August 12, 2013

Ms. Helen Munter, Director
Division of Registration and Inspections
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006

Re: Response to Draft Report on the 2012 Inspection of PricewaterhouseCoopers LLP

Dear Ms. Munter:

We are pleased to provide our response to the Public Company Accounting Oversight Board's ("PCAOB" or the "Board") Draft Report on the 2012 Inspection of our Firm's 2011 audits (the "Report").

We continue to support the PCAOB's mission and we value the insights provided by the PCAOB's inspection process. We personally and our partners collectively are committed to addressing the issues identified in the Report in a thorough and thoughtful manner.

We have evaluated each of the observations set forth in *Part I - Inspection Procedures and Certain Observations* of the Report and taken appropriate actions under both PCAOB standards and our policies. Our evaluation included those steps that we considered necessary to comply with AU 390, *Consideration of Omitted Procedures After the Report Date,* and where applicable, AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*.

We believe that as with any audit process, judgments are necessarily involved in the inspection process and professionals can reach different conclusions about the adequacy of audit evidence in a particular circumstance. In those instances where such differences exist related to the inspection observations detailed in this Report, they generally related to the significance of the observation in relation to the audit evidence taken as a whole rather than the specific nature of the observation. So, while we may disagree with the significance of inspection observations in certain cases, we have taken all of the Board's observations into account in formulating our plan to continuously improve audit quality.

Consistently performing high-quality audits, and in doing so, meeting the needs and expectations of our stakeholders, including the PCAOB, is the top priority of our partners. We look forward to continuing our dialogue with the PCAOB in support of our priority commitment to audit quality.

We would be pleased to discuss any aspect of our response or any further questions you may have.

Sincerely,

Bob Moritz
US Chairman and Senior Partner
PricewaterhouseCoopers LLP

Vincent Colman
US Assurance Leader
PricewaterhouseCoopers LLP