PCAOB Cross-Border Enforcement

March 30, 2017

Continuing its regulatory focus on cross-border audits on both the inspection and enforcement fronts, the PCAOB announced on March 29, 2017 that it had settled charges against two former partners of Brazil-based Deloitte Touche Tohmatsu Auditores Independentes for failure to cooperate with a PCAOB inspection and investigation. In addition, on February 9, 2017 the PCAOB imposed sanctions on KAP Purwantono, Sungkoro & Surja ("EY-Indonesia"), an engagement partner, and an EY Area Professional Practice Director ("Area PPD") for audit failures and failure to cooperate with a PCAOB inspection and investigation.

The action against the two former Deloitte Brazil partners follows from its investigation of charges arising out of Deloitte Brazil's 2009 and 2010 audits of a Brazilian airline, Gol Linhas Aéreas Inteligentes S.A. ("Gol"). That investigation previously led to a record $8 million civil penalty against Deloitte Brazil and the imposition of sanctions against 12 former partners and other audit personnel of the firm. In the current PCAOB action, a former chairman of Deloitte Brazil's Policy Committee was censured, fined $35,000, and barred from being an associated person of a registered public accounting firm for failing to take steps to halt Deloitte Brazil's noncooperation after learning that it had improperly altered work papers produced to the PCAOB and continued to provide false documents and information to the PCAOB. The other partner, a former CEO and Managing Partner of Deloitte Brazil, received similar sanctions, but no civil money fine, for refusing to appear for testimony as required by an accounting board demand.

The sanctions against EY-Indonesia arose out of the PCAOB's inspection of EY-Indonesia's audit of PT Indosat Tbk's December 31, 2011 financial statements. As found by the PCAOB, during the 2011 audit, the partner responsible for performing the cross-border regulatory review of the Indosat audit expressed concern to the engagement partner regarding the sufficiency of Indosat's analysis of over 4,000 leases related to spaces, or "slots," on cellular towers. The engagement team made repeated requests to management, but failed to obtain and evaluate a completed analysis to support the accounting for the leases. Despite the review partner's concerns, the engagement partner obtained authorization from the EY Area PPD for the Asia-Pacific region to release the audit report subject to obtaining a completed analysis in the near future and explaining to Indosat management that the support ultimately obtained could require a restatement of Indosat's financial statements. An appropriately supported lease analysis was not completed until later—February 2013.

When EY-Indonesia learned that the 2011 Indosat audit would be subject to PCAOB inspection, the audit work papers had not yet been archived. Although under PCAOB standards the audit documentation was to be completed by June 13, 2012, the work papers were not archived until July 16, 2012. Nevertheless, according to the PCAOB's findings, over the next five months, engagement team members continued to create or modify and add without proper disclosure, dozens of documents to multiple areas of the 2011 audit work papers. During the investigation that followed, the engagement partner, under oath, failed to disclose his knowledge that an audit memo had been improperly prepared during the PCAOB inspection or his involvement in the memo's improper preparation. And a member of EY-Indonesia's senior leadership did not promptly follow up on information received in an internal investigation about the engagement partner's involvement, instead informing the PCAOB staff that no evidence existed that any senior personnel, including the engagement partner, knew of or participated in the improper conduct. As a result, the PCAOB censured the firm, the engagement partner, and the Area PPD $1,000,000, $20,000, and $10,000, respectively. In addition, the engagement partner was barred from being associated with a registered public accounting firm, and the Area PPD was prohibited from serving in certain capacities in any audit for a one year period.

Conclusion

As we have previously noted, audit firms involved in cross border audits, whether they be foreign audit firms or U.S. based audit firms, should expect the continued focus of the PCAOB in the coming year and beyond. PCAOB chairman, James R. Doty, reiterated the point in the Board's February 9, 2017 news release, "PCAOB standards and oversight are key protections for investors in U.S. securities. Wherever located, all audit firms that elect to register with the PCAOB must ensure that they and their personnel comply and cooperate with PCAOB inspections and investigations." **PCAOB News Release**

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