UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 56469 / September 19, 2007

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2720 / September 19, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12810

In the Matter of

ROBERT M. HARBRECHT, CPA, and
BRIAN R. SPIRES, CPA

Respondents.

ORDER INSTITUTING PUBLIC ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that public administrative proceedings be, and hereby are, instituted against Robert M. Harbrecht, CPA ("Harbrecht") and Brian R. Spires, CPA ("Spires"), pursuant to Rule 102(e)(1)(ii) of the Commission's Rules of Practice.[1]

[1] Rule 102(e)(1)(ii) provides, in pertinent part, that:

> The Commission may . . . deny, temporarily or permanently, the privilege of appearing or practicing before it . . . to any person who is found . . . to have engaged in unethical or improper professional conduct.

II.

In anticipation of the institution of these proceedings, Respondents have each submitted an Offer of Settlement ("Offers") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over them and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Public Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondents' Offers, the Commission finds[2] that:

A. SUMMARY

1. These proceedings concern the improper professional conduct, within the meaning of Commission Rule 102(e)(1)(iv)(B)(2), of Robert M. Harbrecht and Brian R. Spires (collectively the "Respondents") in connection with the audit of the 2000 consolidated financial statements ("2000 audit") of National Century Financial Enterprises, Inc. ("NCFE"), a Dublin, Ohio privately owned healthcare finance company. Harbrecht was the engagement partner for Deloitte & Touche LLP's ("Deloitte") audits of NCFE for the years ended 1999 through 2001, and Spires was the engagement manager for the 1999 and 2000 year-end audits. Deloitte completed the 2000 audit in May 2001.

2. NCFE operated programs through which special purpose subsidiaries conducted private placement note offerings, the proceeds of which were used to purchase healthcare receivables. NCFE represented to the note holders that NCFE would use the proceeds from the note offerings exclusively for the purchase of patient-specific healthcare accounts receivable. Although NCFE used note holder funds to purchase healthcare accounts receivable, NCFE used a substantial portion of the private placement proceeds to make either unsecured loans or loans secured by collateral other than healthcare accounts receivable ("non-permitted advances"), contrary to NCFE's representations to note holders and contrary to the requirements of the master trust indentures ("indentures") that governed NCFE's programs. The quality of the receivables purchased in the programs was material to note holders because the pool of purchased receivables was the sole source from which note holders would be repaid. As part of a complex scheme, NCFE concealed its non-permitted uses of note holder funds by, among other things, making false and misleading statements in its annual financial statements, including in the 2000 consolidated financial statements ("2000 Financials") and by making false and misleading statements to its note holders, the program trustees, rating agencies, and the auditors.

[2] The findings herein are made pursuant to Respondents' Offers of Settlement and are not binding on any other person or entity in this or any other proceeding.

3. As the engagement partner, Harbrecht signed an unqualified audit report for the 2000 audit and had overall responsibility for the planning and execution of the 2000 audit. As the engagement manager, Spires also participated in the planning and execution of the 2000 audit. Respondents failed to plan and execute the 2000 audit in accordance with generally accepted auditing standards ("GAAS"). They failed to obtain sufficient competent evidential matter to corroborate that NCFE's receivables portfolio consisted of purchased healthcare accounts receivables or to properly evaluate the adequacy of NCFE's allowance for losses relating to those receivables. Respondents also did not properly evaluate red flags during the audit which should have alerted them to NCFE's non-permitted advances and its borrowers' inability to repay those advances. Additionally, Respondents failed to obtain sufficient competent evidential matter with regard to the nature and substance of material related party transactions. Many of these transactions with related parties were non-permitted advances.

4. These audit deficiencies caused Harbrecht to sign an unqualified audit report that erroneously stated that NCFE's 2000 Financials were prepared in accordance with generally accepted accounting principles ("GAAP") and that Deloitte conducted its audit in accordance with GAAS. Respondents engaged in improper professional conduct as defined in Rule 102(e)(1)(iv)(B)(2) of the Commission's Rules of Practice in connection with the 2000 audit.

B. RESPONDENTS

5. Robert M. Harbrecht, age 57, of Worthington, Ohio, joined Deloitte as an auditor in 1972 and was a partner from 1984 until he retired in 2004. Harbrecht is a certified public accountant in the state of Ohio and was licensed in Ohio until he allowed his license to lapse in early 2006. Harbrecht served as the engagement partner on the 1999 through 2001 audits of NCFE. At the time of the NCFE audits, Harbrecht had more than twenty-five years of auditing experience, including extensive experience in the financial services industry, and he served on Deloitte's National Banking Committee.

6. Brian R. Spires, age 47, of New Albany, Ohio, joined Deloitte as an auditor in 1988 and was a senior manager from 1998 until he left Deloitte in 2001. Spires is a licensed certified public accountant in the state of Ohio. Spires served as the manager on the 1999 and 2000 audits of NCFE. At the time of the NCFE audits, Spires had more than ten years of auditing experience, with a specialization in the financial services industry.

C. OTHER RELEVANT ENTITY

7. **Deloitte & Touche LLP** is a Delaware limited liability partnership whose principal offices are located in New York, New York. Deloitte provides, among other things, audit assurance and business advisory services. Deloitte has numerous branches domestically and abroad, including a branch in Columbus, Ohio. Deloitte served as auditor for NCFE for the 1999 to 2001 audits.

D. FACTS

NCFE Background

8. NCFE was an Ohio corporation with its principal place of business in Dublin, Ohio until it filed for bankruptcy in November 2002. From 1991 through 2002, NCFE operated programs through which special purpose subsidiaries purchased medical accounts receivable from healthcare providers. The programs raised funds for the purchase of accounts receivable through private offerings of highly rated debt securities to institutional investors ("note holders" or "investors"). NCFE represented to note holders that the programs would use the note proceeds exclusively to purchase patient-specific medical accounts receivable from healthcare providers. The programs and note offerings were structured as asset-backed securitizations, with the notes being fully collateralized by the purchased medical accounts receivable and cash reserves held in the programs. From 1991 through 2002, NCFE's subsidiaries issued more than $17 billion in asset-backed bonds or notes through private placements.

9. NCFE's programs were set out in a series of agreements between the special purpose subsidiaries, healthcare providers, program trustees, and note holders, including, among other things, an indenture which outlined the respective parties' rights and obligations. The indentures allowed the programs to engage only in one type of business activity: the purchase of "eligible" medical accounts receivable of a hospital, physicians' group, or other healthcare provider. Eligible receivables were defined to include only the insured portion of a receivable for which medical services had already been rendered. The program agreements required that the special purpose subsidiaries purchase receivables at a price equal to 97% of the receivables' estimated collectible value.

10. The indentures also placed certain requirements on the programs that were designed to protect note holders from loss. Failure to comply with certain key provisions of the indentures constituted an event of default. If NCFE could not cure the defaults within a specified time period, the indentures required the program trustees to declare a principal amortization event. Such an event would cause the program to cease purchasing receivables and would result in an immediate liquidation of the program. For example, to ensure that the programs had sufficient collateral to cover the outstanding notes, the indentures required the programs to maintain at all times cash reserves and eligible receivables equal to at least 111% of the amount of notes outstanding ("collateral coverage test").[3] If the collateral dropped below 111% for more than seven days, the notes were immediately callable and the indentures required the programs to be immediately liquidated. The indentures also required healthcare providers to immediately replace receivables older than 180 days ("defaulted receivables") with new eligible receivables. If they did not, the value of the defaulted receivables was to be deducted from the next funding to that provider, and the defaulted receivables could not be counted as eligible collateral for purposes of the collateral coverage test.

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[3] NCFE withheld 17% of the purchase price of eligible receivables as a safeguard against non-collection, and held this money as collateral in the form of cash reserves for the program note holders.

11. The indentures required an annual audit of NCFE's consolidated financial statements. NCFE's audited financial statements were provided to the program trustees, the rating agencies that rated the notes, and were provided to investors upon request. Deloitte served as auditor of NCFE's consolidated financial statements for the years ended 1999 through 2001. Harbrecht was Deloitte's engagement partner for the 1999 through 2001 year-end audits, and Spires was Deloitte's engagement manager for the 1999 and 2000 audits. Harbrecht signed unqualified audit reports on NCFE's 1999 and 2000 financial statements. He did not sign an audit report on the 2001 financial statements because Deloitte did not complete its audit for that year.

NCFE'S Misuse of Note Proceeds and Misrepresentations

12. From at least 1994 until 2002, NCFE diverted note holder funds to make unsecured loans or loans secured by collateral other than eligible healthcare receivables. This practice contradicted the requirements of the trust indentures and NCFE's representations to investors that NCFE was to use note holder funds exclusively for the purchase of eligible healthcare receivables. NCFE used note holder funds to provide funding to healthcare providers that had already sold all of their medical accounts receivables to NCFE and had no additional eligible receivables to sell. Many of these providers had incurred significant operating losses over a period of years and lacked the ability to repay NCFE. NCFE made material non-permitted advances to providers that were owned in part by NCFE or NCFE's principals.

13. NCFE's non-permitted advances had a much higher collection risk than purchased eligible accounts receivable. Because eligible receivables were to be paid by highly rated third-party payers, such as insurance companies, HMOs, and governmental entities such as Medicare and Medicaid, for medical services that had already been rendered and billed to the payers, the eligible receivables were of the highest credit quality. By contrast, it was much less likely that NCFE would be able to collect on non-permitted advances because they were in substance unsecured loans to severely financially distressed borrowers. In fact, NCFE had very poor collection experience on its non-permitted advances, and in some cases NCFE went more than a year without receiving any payments from certain providers.

14. The amount and significance (as a percentage of NCFE's total receivable portfolio) of the non-permitted advances rapidly grew over time. By 2000, non-permitted advances represented more than half of NCFE's entire provider receivable portfolio.

15. NCFE's practice of making non-permitted advances caused the programs to be under collateralized, with eligible receivables plus cash reserves falling well short of the required 111% of the value of the notes. A violation of this covenant required an immediate acceleration in the maturity of the notes and liquidation of the programs.

16. NCFE concealed its non-permitted advances and the resulting indenture violations by making materially false and misleading statements in its 2000 Financials and to its note holders, the program trustees, rating agencies, and the auditors.[4] The 2000 Financials departed from GAAP due to misstatements and omissions relating to NCFE's non-permitted advances. The 2000

[4] There were similar misstatements and omissions in NCFE's earlier financial statements as well.

Financials materially misrepresented that NCFE's receivable portfolio consisted of purchased medical accounts receivable, when in fact more than half of the portfolio consisted of non-permitted advances. Further, NCFE failed to evaluate the impairment present in its receivable portfolio attributable to the non-permitted advances to insolvent providers. NCFE's allowance for losses was grossly inadequate given its non-permitted lending activity. Finally, NCFE failed to disclose that the programs were in default under the indentures and did not have the ability to cure those defaults.

17. Note holders eventually uncovered NCFE's fraud in October 2002. The note holders called the notes, which drove NCFE into bankruptcy in November 2002. By that point, however, most of NCFE's approximately $3 billion of outstanding receivables were unsecured or backed by collateral that was virtually worthless. As a result of NCFE's fraudulent scheme, note holders suffered more than $2 billion in losses. Such losses do not reflect subsequent recoveries from civil litigation.

Deloitte's 2000 Audit of NCFE

18. NCFE's fraud went undetected and investor losses continued to grow from 2000 through 2002. Harbrecht signed an unqualified audit report on NCFE's 2000 Financials. Deloitte's 2000 audit report erroneously stated that the financial statements were prepared in conformity with GAAP and that the audits had been conducted in accordance with GAAS. Respondents were both responsible for the planning and execution of the 2000 audit. Respondents failed to perform certain audit procedures required by GAAS and failed to properly evaluate red flags that could have alerted them to NCFE's non-permitted advances and to the impairment of NCFE's receivable portfolio.

Existence of Purchased Accounts Receivable

19. According to Respondents, NCFE's accounts receivable was one of the most significant areas of the 2000 audit. NCFE had $2.3 billion of accounts receivable outstanding at the end of 2000, which represented 81% of the company's $2.9 billion of total assets. Nevertheless, Respondents failed to obtain evidential matter sufficient to corroborate NCFE's representation in its 2000 Financials that NCFE's receivable portfolio represented purchased patient-specific healthcare receivables. Respondents' failure to obtain sufficient competent evidential matter supporting the purported purchase of accounts receivable resulted in their failure to discover that NCFE's receivables included a significant amount of non-permitted advances for which no purchased patient-specific receivables existed.

20. Respondents devised an internal control reliance strategy in testing NCFE's receivable portfolio for the 2000 audit, placing some reliance on internal controls associated with the processing of funding advances and the remittance of payments made by third party payers. The testing of these controls had been performed during the 1999 audit and was updated subsequently. However, the internal controls testing performed by the engagement team provided insufficient evidence as to the effectiveness of the controls in these areas. The engagement team's internal controls testing consisted of a "walk-through" of NCFE's control environment, which included discussions with NCFE executive and mid-level management personnel, but did not

include the identification of the specific controls that the engagement team intended to rely upon or the specific documents and functions that it would examine in establishing the effectiveness of those controls. Through this walk-through, the engagement team learned about NCFE's purported process of purchasing eligible receivables that supposedly ensured NCFE's receivable portfolio consisted exclusively of purchased eligible receivables. However, Respondents failed to obtain sufficient competent evidential matter to corroborate that NCFE had in fact adhered to its controls and that the controls operated effectively throughout the accounting period. The engagement team instead relied heavily on management's representations as to how the controls were purportedly operating and reviewed an insufficient sampling of documents that did not provide sufficient competent evidential matter of NCFE's purchase of eligible receivables.

21. Respondents also failed to design substantive audit procedures to corroborate the existence of purchased patient-specific accounts receivable. NCFE had three accounting systems: the servicing department's AS400 system that contained all the patient-specific receivable information ("AS400"); the funding department's DMaster system that tracked the amount funded to providers ("DMaster"); and the general ledger. NCFE represented that the funding department was supposed to limit funding to the amount of patient-specific receivables residing in the AS400. In practice, however, NCFE regularly advanced amounts to providers exceeding the amount of patient-specific receivables available for purchase. Respondents decided that the engagement team should select accounts for confirmation using the amounts in the DMaster, based on their erroneous conclusion that the amounts recorded as funded in the DMaster would be equivalent to the amount of accounts receivable recorded in the AS400. However, by using the DMaster amounts, the engagement team merely confirmed the amounts funded to providers, not the amount of purchased patient-specific receivables. Moreover, the confirmations designed by the engagement team asked only that the provider confirm "the balance due" to the NCFE program rather than the amount of patient-specific receivables purchased by the program.

22. Similarly, the engagement team tested only the accounts receivable reconciliations between the DMaster and the general ledger, despite being provided reconciliations for all three systems by NCFE. NCFE prepared detailed account reconciliations for each healthcare provider with which it did business. By testing the DMaster instead of the AS400, the engagement team merely determined that the amount funded to providers, rather than the amount of purchased receivables, reconciled to the general ledger. This procedure did not provide sufficient competent evidential matter concerning the existence of eligible purchased accounts receivable.

23. Respondents did not adequately investigate audit evidence contained in the accounts receivable reconciliation schedules that revealed NCFE's non-permitted lending. The reconciliation schedules showed significant shortfalls in the AS400 compared to the DMaster for some providers due to the non-permitted advances; these advances appeared in the DMaster but had no corresponding patient-specific receivable data in the AS400. In fact, the single largest reconciling item NCFE used to reconcile the AS400 to the DMaster and general ledger was a line item entitled "Amount Over/(Under)Advanced to Seller," which revealed the non-permitted advances to the providers. The reconciliation for one provider showed an amount over-advanced to that provider in excess of $200 million. For another provider, the reconciliation showed a $42.1 million general ledger receivable balance but no AS400 receivable detail, indicating that the entire general ledger amount constituted non-permitted advances.

The Valuation of NCFE's Accounts Receivable

24. Respondents also failed to obtain evidential matter sufficient to support NCFE's valuation of its receivable portfolio. NCFE created an allowance for losses equal to 2% of its receivable portfolio, which was based on its historical charge-off rate for uncollectible accounts. NCFE's allowance for losses was inadequate because of the impairment resulting from non-permitted advances made to financially insolvent providers. The reason NCFE's historical charge-off rate was so low was because NCFE did not charge off most of its impaired receivables.

25. Respondents determined that collectibility was not a significant issue for NCFE's receivable portfolio, based on their understanding of how the programs were supposed to operate and based on management's representations regarding collections. Respondents understood that there was a low risk of collection loss because the receivables were purportedly payable by financially sound third-party insurers and government programs such as Medicare. They also understood that NCFE was required to return 180-day-old receivables to the selling providers, and that NCFE also held back a percentage of the purchase price of the receivables as a safeguard against unanticipated collection losses. Thus, the engagement team accepted NCFE's $43.7 million allowance for losses for its $2.5 billion receivable portfolio. This allowance was intended to cover the estimated losses in the $2.3 billion provider receivable portfolio and the losses associated with $49.7 million of promissory notes from providers that were identified by the engagement team as having a poor collection history. NCFE deducted holdback reserves from provider fundings that could absorb some credit and collection losses; however, these cash reserves were available to cover only a limited percentage of each provider's respective receivables balance.[5]

26. Respondents did not obtain sufficient competent evidential matter to support its conclusion that management's methods for estimating the allowance for credit and collection losses were reasonable. For example, Deloitte's model audit program for the 2000 audit instructed the engagement team to evaluate the reasonableness of management's methods for its estimates of the allowance for losses. The model audit program advised reviewing, among other things, accounts receivable aging. When the engagement team requested a consolidated receivable aging analysis from NCFE, management informed the team that the company could track aging by program only and was incapable of generating a consolidated aging schedule. Respondents accepted this response and did not require NCFE to produce consolidated aging reports or other similar information that would have enabled the engagement team to evaluate the delinquency rate and collection losses in NCFE's portfolio. The engagement team did not perform an analysis of

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[5] NCFE's programs withheld 17% of the amount funded to providers as cash reserves primarily to provide additional collateral for note holders, and secondarily to absorb credit or collection losses in the portfolio. These reserves totaled $332 million at the end of 2000. These reserves could be used on a provider-by-provider basis to absorb the first 17% of losses incurred for a particular provider. However, the reserves for one provider could not be used to absorb losses in another provider's portfolio. Furthermore, in the event of early amortization of NCFE's programs, the cash reserves were to serve as collateral to guard against note holder losses rather than to absorb losses in NCFE's receivable portfolio.

accounts receivable aging, nor did it review other information relating to delinquent accounts receivable for the 2000 audit. The engagement team did not perform other alternative audit procedures to independently assess the reasonableness of the allowance for losses.

27. Respondents relied excessively on management's representations regarding the operation of the NCFE programs and collectibility of the receivables. Respondents also failed to obtain sufficient competent evidential matter to establish that NCFE was requiring providers to replace 180-day-old receivables with new receivables or, alternatively, was deducting the value of the defaulted receivables from future fundings. Respondents thus failed to implement procedures from which Deloitte could have discovered that NCFE had many receivables over 180 days old still on its books.

28. Respondents did not properly evaluate audit evidence that revealed NCFE was experiencing significant delinquencies in the receivable portfolio. For example, NCFE provided Deloitte with summarized statements for each provider that showed account activity during 2000. The engagement team attached these statements to the audit confirmation requests. These statements revealed that NCFE had collected very little from many of its providers during 2000, and in some cases had not made any collections for the entire year. Similarly, each client prepared accounts receivable reconciliation also contained a roll-forward analysis from the 2000 beginning balance to the ending balance. These schedules also showed poor collections.[6] Despite being presented with this information about collections, Respondents did nothing further to reconcile this evidence with their conclusion that the programs were operating as they were designed.

29. Deloitte's audit work on the reconciliations between the general ledger accounts receivable balance and the DMaster balance also raised questions about the collectibility of NCFE's receivables. Respondents learned that NCFE had reclassified $110 million of accounts receivable to notes receivable. The reclassified receivables represented instances where NCFE had poor or no collection activity on receivables, and where NCFE set up a note with the provider to establish a collection schedule. Respondents also became aware that NCFE did not recognize $21 million of program fee revenues because cash collections on the underlying receivables were insufficient to cover the program fees earned on the advances made to those providers. This should have indicated to them that NCFE's receivables portfolio included approximately $200 million of non-performing, delinquent receivables. Respondents did not make additional audit inquiries into these matters or into collections on NCFE's receivables, despite the contradictions between these facts and management's representations about the operation of the programs and the collectibility of NCFE's receivables.

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[6] Deloitte's confirmation sample represented more than 80% of the value of NCFE's receivable portfolio. Thus, the age of receivables in this sample revealed that a significant portion of NCFE's receivables were more than a year old, even though the programs contemplated the receivables turning over every 90 to 120 days.

NCFE's Compliance with Trust Indenture Covenants

30. Respondents were aware that NCFE's programs were in violation of certain provisions of the trust indentures. Although NCFE misleadingly claimed that the indenture violations were not material, the engagement team identified these violations as an area that would require "heightened audit attention."

31. Respondents failed to obtain sufficient competent evidential matter to determine whether NCFE was in compliance with the key provisions of the indentures that could lead to defaults and require liquidation of the programs. Among other things, the engagement team relied on client-prepared investor reports provided to the program trustees on a monthly basis as evidence of NCFE's compliance with certain indenture covenants. Because these reports were prepared by NCFE, they routinely misrepresented that NCFE was in compliance with the most critical terms of the indentures, as NCFE was concealing its violations from the trustees. The engagement team failed to obtain sufficient competent evidential matter to corroborate the accuracy of the data on these reports.

NCFE's Related Party Transactions

32. Respondents identified related party transactions as a risk area that would require attention during the audit. Approximately half of NCFE's receivables portfolio constituted business with related parties, which was the most Harbrecht had ever encountered in an audit.

33. The engagement team's audit procedures for related party transactions were limited to receiving a schedule from NCFE that depicted related party receivable balances and program fees and agreeing such amounts to the associated disclosures in the footnotes to the 2000 Financials. Respondents relied on management's representations that NCFE had made these related party advances pursuant to the terms and requirements of the programs. Respondents did not scrutinize these transactions in order to understand the nature and business purpose of the transactions, notwithstanding the high concentration of business with related parties. Respondents also failed to obtain information about the financial condition of non-consolidated related parties to determine whether NCFE was avoiding the recognition of losses associated with these business relationships. Further analysis by the engagement team could have revealed that a significant portion of the business conducted with related parties represented non-permitted advances for which the providers did not have the financial capacity to repay. It also could have revealed that, despite the lack of collections, NCFE was continuing to make unsecured advances to these related parties.

34. Furthermore, NCFE's three largest related party relationships constituted 46% of its entire $2.4 billion receivable portfolio at the end of 2000. The engagement team failed to evaluate the risk associated with this concentration of receivables among only a few providers, despite those providers being related parties.

Departures from GAAS

35. The third standard of field work requires that an auditor must obtain "sufficient competent evidential matter" to provide "a reasonable basis for an opinion regarding the financial statements under audit." (AU § 326, Evidential Matter, at AU 326.01) GAAS further states that "representations from management are part of the evidential matter the independent auditor obtains, but they are not a substitute for the application of those auditing procedures necessary to afford a reasonable basis for an opinion regarding the financial statements under audit." (AU § 333, Management Representations, at AU 333.02) The third general standard requires that "[d]ue professional care is to be exercised in the planning and performance of the audit and the preparation of the [audit] report." (AU § 230, Due Professional Care in the Performance of Work, at AU 230.01) "Due professional care requires the auditor to exercise *professional skepticism*," (AU 230.07), and "[i]n exercising professional skepticism, the auditor should not be satisfied with less than persuasive evidence because of a belief that management is honest." (AU 230.09) "The auditor obtains written representations from management to complement other auditing procedures." (AU 333.03)

36. Respondents placed too much reliance on management's representations regarding the operation of NCFE's programs, which led to improper assumptions in several audit areas. Based primarily on management representations, Respondents improperly concluded that all of NCFE's funding to providers represented eligible purchased patient-specific accounts receivable. This caused them to erroneously utilize the funding department's system for confirmation and reconciliation procedures instead of the servicing department's system, which contained the patient-specific accounts receivable detail. Respondents failed to obtain sufficient competent evidential matter to corroborate that NCFE had actually purchased patient-specific receivables from providers. Respondents also relied heavily on management's representations regarding the operation of the programs in concluding that NCFE had a low risk of credit and collection losses. As a result, they decided to forgo performing certain audit procedures designed to corroborate the reasonableness of management's assumptions underlying its estimates of the allowance for losses. Respondents failed to obtain sufficient competent evidential matter and failed to exercise due professional care and professional skepticism when auditing the existence and valuation of NCFE's receivable portfolio.

37. Furthermore, Respondents failed to obtain sufficient competent evidential matter to verify NCFE's compliance with key provisions of the trust indentures. They instead relied on client-prepared monthly investor reports without adequately corroborating the veracity of the data in those reports. Thus, Respondents failed to obtain sufficient competent evidential matter to conclude that NCFE was in compliance with the most significant provisions of the trust indentures.

38. GAAS states that the purpose of assessing control risk during an audit "is to contribute to the auditor's evaluation of the risk that material misstatements exist in the financial statements." (AU § 319, Consideration of Internal Control in a Financial Statement Audit[7], at AU

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[7] AU 319 was modified by Statement on Auditing Standards No. 94, The Effect of Information Technology on the Auditor's Consideration of Internal Control in a Financial Statement Audit, which was integrated into AU 319 in May 2001 and applied to audits of financial statements for

319.79 (pre-amendment), AU 319.105 (post-amendment)) When the auditor intends to place reliance on internal controls, the auditor must identify specific controls that are relevant to specific assertions in the financial statements and perform tests of those controls. (AU 319.48 (pre-amendment), AU 319.70 (post-amendment))

39. Respondents failed to design audit tests of internal control procedures sufficient to justify the amount of reliance the engagement team placed on NCFE's internal controls in connection with auditing NCFE's accounts receivable. With regard to NCFE's receivable portfolio, Respondents failed to identify specific controls that Deloitte would rely upon with respect to specific assertions in NCFE's financial statements and failed to obtain sufficient competent evidential matter to establish the operating effectiveness of those controls.

40. GAAS states that, when testing the effectiveness of internal controls through observation, the auditor should consider "that the observed application of a control might not be performed in the same manner when the auditor is not present." (AU 319.68 (pre-amendment), AU 319.94 (post-amendment)) Observation therefore "may be insufficient to evaluate the effectiveness of the design or operation of controls for periods not subjected to [observation]. In such circumstances, the auditor may decide to supplement [observation] with other tests of controls that are capable of providing evidential matter about the entire audit period." (AU 319.70 (pre-amendment), AU 319.96 (post-amendment))

41. Respondents failed to design adequate internal control testing procedures to ensure that NCFE's internal controls operated effectively throughout the audit period. By making corroborative inquiries as to the operation of controls and by observing NCFE's various control functions, the engagement team obtained an understanding of the design of NCFE's controls. However, Respondents failed to obtain sufficient competent evidential matter that the controls were operating effectively at all times during the audit period, such as tests of those controls at different times throughout the audit period.

42. GAAS states that "for evidence to be competent, it must be reliable and relevant. The relevance of evidence depends on its relationship to the financial statement assertion being addressed." (AU § 330, The Confirmation Process, at AU 330.11) When designing confirmation requests, "the auditor should consider the assertion(s) being addressed and the factors that are likely to affect the reliability of the confirmations." (AU 330.16) An auditor should consider factors such as a confirmation respondent's motivation, objectivity, and freedom from bias when designing confirmation requests, and should consider whether other procedures are necessary as a result. (AU 330.27) Furthermore, "there may be circumstances . . . in which the auditor should exercise a heightened degree of professional skepticism relative to these factors", such as "where the confirmation respondent is the custodian of a material amount of the audited entity's assets." (Id.)

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periods beginning on or after June 1, 2001. These amendments did not apply to the 2000 NCFE audit. Therefore, all citations to AU 319 will include the pre-amendment citation in effect at the time of the audit, as well as the post-amendment citation to the current AU 319.

43. Respondents failed to design confirmation requests tailored to the audit objective of confirming management's financial statement assertion that its receivables constituted eligible purchased patient-specific receivables. The confirmations requested that the provider confirm the "balance due" NCFE instead of the amount of patient-specific receivables NCFE had purchased from the provider. Thus, Deloitte confirmed only the amount funded by NCFE to a particular provider, not the amount of purchased receivables. Based on management's representations and reliance on internal control testing, Respondents decided their confirmation approach was acceptable because they incorrectly concluded that the amount funded by NCFE in all cases equaled the amount of eligible patient specific receivables NCFE had purchased. Furthermore, Respondents failed to exercise the necessary level of professional skepticism by placing too much reliance on confirmation responses from customers in which NCFE had an ownership interest or which were financially dependent on NCFE, and which also were custodians of a significant portion of NCFE's assets. Respondents did not sufficiently evaluate whether these confirmation responses would provide competent evidence given that NCFE was the primary funding source for many of its providers. The engagement team did not obtain sufficient competent evidential matter about the providers' operating histories or their financial condition in order to assess whether those providers were subject to improper influence by NCFE.

44. GAAS states that "[i]f a representation made by management is contradicted by other audit evidence, the auditor should investigate the circumstances and consider the reliability of the representation made. Based on the circumstances, the auditor should consider whether his or her reliance on management's representations relating to other aspects of the financial statements is appropriate and justified." (AU 333.04)

45. Respondents gathered audit evidence during the 2000 audit that should have caused them to question management's representations about the operations of the programs and to reevaluate their conclusions as to the existence of purchased accounts receivable and as to the credit and collection risk for NCFE's receivables. Most notably, they became aware that NCFE had required providers to provide notes receivable to secure $110 million of delinquent accounts receivable. Respondents also became aware that NCFE did not recognize $21 million of program fee revenues because cash collections on the underlying receivables were insufficient to cover the program fees earned on the advances made to those providers. This should have indicated to them that NCFE's receivables portfolio included approximately $200 million of non-performing, delinquent receivables. Respondents failed to exercise professional skepticism when faced with these facts. At a minimum, they should have questioned why, despite these collection issues, NCFE did not create a specific allowance for or write off these receivables.

46. GAAS states that an auditor should "be aware of the possibility that transactions with related parties may have been motivated solely, or in large measure, by conditions" such as, among other things, the "[l]ack of sufficient working capital or credit to continue the business." (AU § 334, Related Parties, at AU 334.06) "The auditor should place emphasis on testing material transactions with [related parties]." (AU 334.07) "The auditor should apply the procedures he considers necessary to obtain satisfaction concerning the purpose, nature, and extent of [related party] transactions and their effect on the financial statements." (AU 334.09) "The procedures should be directed toward obtaining and evaluating sufficient competent evidential matter and should extend beyond inquiry of management." (Id.) Such procedures may include inspecting or

confirming the value of collateral in the transaction. (Id.) When necessary to fully understand a particular transaction, if there are material uncollected balances, an auditor should consider obtaining information about the financial capability of the other party to the transaction. (AU 334.10) "The higher the auditor's assessment of risk regarding related party transactions, the more extensive or effective the audit tests should be." (AU § 9334, Related Parties – Auditing Interpretations of Section 334, at AU 9334.19) To understand a related party transaction, or obtain evidence regarding it, "the auditor may have to refer to . . . financial statements of the related party." (Id.)

47. Respondents did not perform audit procedures necessary to understand and test the terms of NCFE's related party transactions. This was especially significant because approximately half of NCFE's business was with related parties. The risk associated with NCFE's related party transactions was further exacerbated because 46% of NCFE's receivable portfolio was concentrated in three related parties. A careful review of NCFE's relationships with these three related parties would have revealed that these customers were severely financially distressed and were receiving unsecured loans from NCFE to fund their operating losses. Despite this material concentration risk, Respondents failed to properly scrutinize NCFE's related party transactions.

E. RULE 102(e)

48. Rule 102(e)(1)(ii) of the Commission's Rules of Practice states, in pertinent part, that, "[t]he Commission may . . . deny, temporarily or permanently, the privilege of appearing or practicing before it in any way to any person who is found . . . to have engaged in unethical or improper professional conduct." With respect to persons licensed to practice as accountants, such as Respondents, "improper professional conduct" under Rule 102(e)(1)(ii) includes, among other things, the following type of negligent conduct: "repeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards, that indicate a lack of competence to practice before the Commission". (Rule 102(e)(1)(ii)(B)(2))

49. As described above, Respondents engaged in improper professional conduct in connection with the 2000 audit. Respondents negligently failed to conduct the 2000 audit of NCFE in conformity with the requirements of GAAS. Harbrecht and Spires engaged in repeated instances of unreasonable conduct, which resulted in violations of GAAS, and which indicate a lack of competence to practice before the Commission.

F. FINDINGS

Based on the foregoing, the Commission finds that Respondents engaged in improper professional conduct pursuant to Rule 102(e)(1)(ii) of the Commission's Rules of Practice.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondents' Offers.

Accordingly, it is hereby ORDERED, effective immediately, that:

A. Harbrecht is denied the privilege of appearing or practicing before the Commission as an accountant.

B. After eighteen months from the date of this order, Harbrecht may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such an application must satisfy the Commission that Harbrecht's work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Harbrecht, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Harbrecht, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in Harbrecht's or the firm's quality control system that would indicate that Harbrecht will not receive appropriate supervision;

(c) Harbrecht has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Harbrecht acknowledges his responsibility, as long as he appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

C. The Commission will consider an application by Harbrecht to resume appearing or practicing before the Commission provided that his state CPA license is current and he has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will

consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Harbrecht's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

D. Spires is denied the privilege of appearing or practicing before the Commission as an accountant.

E. After one year from the date of this order, Spires may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such an application must satisfy the Commission that Spires' work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Spires, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Spires, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in Spires' or the firm's quality control system that would indicate that Spires will not receive appropriate supervision;

(c) Spires has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Spires acknowledges his responsibility, as long as he appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

F. The Commission will consider an application by Spires to resume appearing or practicing before the Commission provided that his state CPA license is current and he has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will

consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Spires' character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Nancy M. Morris
Secretary