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THE INSTITUTE OF CHARTERED ACCOUNTANTS OF ONTARIO

DISCIPLINE COMMITTEE - ICAO

ROBERT A. SHANKS

IN THE MATTER OF:

DRAFT ALLEGATIONS AGAINST
ROBERT A. SHANKS, CPA, CA, A
MEMBER OF THE INSTITUTE, BEFORE
THE DISCIPLINE COMMITTEE

EX. 2 FILED APRIL 23 2013

ADW

SETTLEMENT AGREEMENT

made pursuant Section 34 (1)(c) of the Chartered Accountants Act, 2010, and to ICAO Regulation 7-1, s. 22.4

Background

1. The Professional Conduct Committee ("PCC") approved the drafting of allegations against Robert A. Shanks ("Shanks" or "the member"). **Schedule "A"**
2. Shanks obtained his BA in Economics from the University of Waterloo in 1972 and he received his CA designation in 1978. He practiced as a sole practitioner from 1979 to 1993 focusing primarily on tax preparation for farming clients. From 1993 to November, 2006 Shanks was involved in various ventures, most recently as the CFO for a public fishery company, and then two years tax consulting for Union Gas. In November, 2006 Shanks opened his current practice in Tilbury, Ontario which consists of himself as a sole practitioner and three employees.
3. Shanks' current practice is 20% tax preparation work, 55% notice to reader statements and 25% review engagements.
4. The Practice Inspection Committee, after their inspection in January of 2009 provided Shanks with an example quality control manual. Shanks deleted reference in the manual to file quality reviews and the monitoring and hiring of specialists or consultants. Shanks removed reference to the hiring of an external monitor or

having a file quality review as he believes he is currently receiving a peer review of his practice through Practice Inspection. It is agreed that a practice inspection does not amount to quality review of assurance files.

5. On April 13, 2012 the Practice Inspection Committee referred Shanks to the Professional Conduct Committee after conducting a third re-inspection and finding continued failures to maintain professional standards.
6. The references to "Doc" numbers are references to documents in the Document Brief attached to this Settlement Agreement. The references to "**Tab**" numbers are references to authorities found in the Standards Brief.

The First Allegation

Robert A. Shanks, in or about the period July 1, 2011 through November 30, 2011, while engaged to perform a review of the financial statements of "Ltd." for the year ended July 31, 2011, failed to perform his professional services in accordance with generally accepted standards of practice of the profession, contrary to Rule 206.1 of the Rules of Professional Conduct.

The Second Allegation

Robert A. Shanks, in or about the period March 1, 2012 through July 31, 2012, while engaged to perform a review of the financial statements of "Ontario Ltd." for the year ended March 31, 2012, failed to perform his professional services in accordance with generally accepted standards of practice of the profession, contrary to Rule 206.1 of the Rules of Professional Conduct.

The Third Allegation

Robert A. Shanks, in or about the period December 1, 2011 through April 30, 2012, while engaged to perform a review of the financial statements of "Farm Inc.", for the year ended December 31, 2011, failed to perform his professional services in accordance with generally accepted standards of practice of the profession, contrary to Rule 206.1 of the Rules of Professional Conduct.

7. CICA Handbook sections 8100 and 8200 **Tab 1 & 2** set out the standards for the review of financial statements by public accountants. Each of the files which are the subject of this Settlement Agreement are review engagements.
8. For each review engagement the public accountant is required to assess whether the information being reported on is plausible (CICA 8100.15) **Tab 1**.

The Particulars to the Allegations

Financial Statements of Ltd. for the year ended July 31, 2011

Allegation 1 (a) he failed to carry out sufficient appropriate analytical procedures to support the plausibility of information contained in the financial statements.

9. The financial statements prepared by the member were relied upon by the bank to support the bank loan of \$940,000 as noted in the working papers Doc p. 5.
10. Inventory is the single largest asset at \$1.3 million or 45% of the assets in 2011 Doc p. 5. While the working papers note that the client performs a physical inventory count Doc p. 15, there is no attendance by the member and no other procedures are undertaken. This is an inadequate procedure given the materiality of inventory to the financial statements.

11. The balance sheet contains an item "prepaid expenses \$189,109" Doc p. 5 which includes prepaid advertising that accumulated in the period 2004 through 2011. 10% of the prepaid amount from 2004 through 2007 was amortized each year. The value of the remaining prepaid advertising is questionable since the company is capitalizing advertising and calling it a current prepaid. Shanks agrees that he did not carry out sufficient appropriate analytical procedures to support the plausibility of the prepaid advertising amount included in prepaid expenses.
12. The balance sheet also contains the item "research and development (Note 5) \$515,036" Doc p. 5. This relates to research into corn and soya beans. There is no analysis as to the assessment of the value of these amounts and no determination that the amount is plausible.
13. The statement of income Doc p. 7 is supported only by ledger details printed from the client's system which list the transactions recorded in certain of the expense accounts Doc pp. 16-24. No review procedures were performed on these accounts.
14. Once Shanks was satisfied with the balance sheet he assumed the income statement was correct. This assumption cannot reasonably be made.
15. While the working paper file contained a letter of representation Doc p. 25, the letter was dated October 15, 2011, two weeks before the date of the report. Representation letters must be obtained as at the date of the report (CICA 8200.35) **Tab 2**
16. Although the planning section of the file contains a working paper with ratios calculated by the Pendock AFP and Excel based working paper software ("AFP system") Doc pp. 27-28, there is no evidence that work was performed on the results. In order to comply with standards for a review engagement (CICA 8100.15 (iii) (a), 8100.19 (b)) **Tab 1**, analysis of these ratios is a primary form of evidence.

Allegation 1 (b) he failed to assess materiality.

17. A materiality worksheet is included in the working paper file Doc pp. 29-30. This worksheet is not filled in and Shanks did not set an amount as materiality.
18. Eight journal entries were prepared in 2011 Doc pp. 31-32. Two items totaling \$5,681.62 Doc p. 33 were not adjusted and two other amounts noted in the working paper files should have been taken to the summary of unadjusted items but were not. By way of example a non-reconciled difference appears in the accounts receivable as an overstatement of the acreage fee of \$1,843 Doc p. 34 and an overstatement of grain payable of \$1,839 Doc p. 35. Because there was no calculation on materiality Shanks could not be certain whether these items should have been adjusted.

Allegation 1 (c) he failed to ensure disclosure of the fact that accounts receivable and inventory were pledged on security of bank indebtedness in the amount of \$940,000.

19. One of the procedures on Shanks' review program was to "inquire and document whether receivables have been pledged, discounted, factored or otherwise encumbered" Doc p. 37. Beside this item Shanks has written "N/A".
20. Both the accounts receivable and inventory were pledged as security on the current bank loan of \$940,000 Doc p. 5. The financial statements should have, but did not, include a footnote disclosing the pledging of these assets. (CICA 3862.14) **Tab 3**

Allegation 1 (d) he failed to carry out sufficient appropriate analytical procedures to support the plausibility of the balance sheet item "Research and Development (Note 5) 515,036".

21. In 2011 research and development costs amounted to \$515,036 Doc p. 5. These were research costs incurred with respect to corn and soya beans.

22. There is no analysis in the working paper file with respect to the value of these amounts and it is agreed that Shanks failed to properly satisfy himself as to the plausibility of this balance sheet item.

Allegation 1 (e) he failed to ensure disclosure of the revenue recognition policy

23. The revenue recognition policy is not disclosed in the notes to the financial statements Doc p. 9 as required (CICA Handbook 3400.21) **Tab 4** and 1505.10 **Tab 5**

Allegation 1 (f) he failed to ensure disclosure of Scientific Research Tax Credits in the period they were earned.

24. CICA Handbook s. 3805.12 **Tab 6** provides that investment tax credits should be accounted for using the cost reduction approach. Shanks was incorrectly accounting for investment tax credits in the period they were earned.

Allegation 1 (g) he failed to ensure disclosure of the terms and conditions of related party transactions.

25. Note 7 to the financial statements Doc p. 11 refers to related party transactions. CICA Handbook s. 3840.51 **Tab 7** requires disclosure of the terms and conditions of related party transactions. While the balance due to and from related parties and the transactions that occurred during the year were disclosed, the terms and conditions were not.

Allegation 1 (h) he failed to ensure disclosure of the fair value of financial instruments.

26. CICA Handbook s. 3856.38(b) **Tab 8** requires disclosure of the fair value of financial instruments. While there is a note for financial instruments Doc p. 10 there is no comment on the fair value.

Allegation 1 (i) he failed to document matters important to support the review engagement report.

27. Generally accepted standards of practice require the member carrying out a review to document matters important to support the review engagement report (CICA 8100.15 review standards, 8100.19-22 review procedures). **Tab 1**
28. There was no documentation of any consideration of materiality.
29. With respect to inventory, Shanks did have discussions with his client as to the reasonableness of the existence and value of inventory but did not document in the working paper files any of these discussions.
30. The working paper file contains a list of four questions to be discussed with the client Doc p. 38. Although there is evidence that Shanks did discuss these matters with the client, there is insufficient documentation in the working paper file as to the resolution of these matters.
31. Generally, Shanks did not document inquiry and discussions that he may have had with the client with respect to financial statement items.

**Financial Statements for Ontario Ltd. for the year ended
March 31, 2012**

Allegation 2 (a) he failed to carry out sufficient appropriate analytical procedures to support the plausibility of information contained in the financial statements.

32. This company is a funeral home with a March 31 year end. Shanks issued a review engagement report without reservation for the March 31, 2012 year end Doc p. 44.
33. Evidence of analytical procedures was inadequate in the 2012 working paper files. With respect to financial statement ratios Doc pp. 53-54, Shanks concluded that ratios were not relevant. In order to comply with standards for a review engagement

(CICA 8100.15 (iii) (a), 8100.19 (b)) **Tab 1**, analysis of these ratios is a primary form of evidence.

Allegation 2 (b) he failed to assess materiality.

34. Although a materiality worksheet is included in the 2012 files Doc pp. 55-56, it is not filled in and Shanks did not set an amount as materiality.

Allegation 2 (c) he failed to ensure disclosure of the terms and conditions of related party transactions.

35. While there is a note to the financial statements regarding related parties and their transactions Doc p. 51, the note does not disclose the terms and conditions as required (CICA Handbook 3840.51) **Tab 7**.

Allegation 2 (d) he failed to ensure disclosure of the fair value of financial instruments.

36. CICA Handbook s. 3856.38(b) **Tab 8** requires disclosure of the fair value of financial instruments. While there is a note for financial instruments Doc p. 50 there is no comment on the fair value.

Allegation 2 (e) he failed to document matters important to support the review engagement report.

37. Generally accepted standards of practice require the member carrying out a review to document matters important to support the review engagement report (CICA Handbook 8100.15 review standards, 8100.19-22 review procedures). **Tab 1**

38. With respect to the balance sheet item "Goodwill (Note 5) \$44,000" Doc p. 45 the working papers indicated that there was no impairment of goodwill Doc p. 57. No documentation is contained in the working paper file to demonstrate how that conclusion was reached.

39. The working paper files contain very limited analysis on the income statement Doc p. 59. Shanks indicated that he does perform analysis of the income statements but there was no documentation in the file.
40. Generally inquiry and analytical procedures were either not completed or not documented on this file. There was no documentation of client inventory count procedures and no documentation of commitment contingencies and subsequent events.

Financial Statements of Farm Inc. for the year ended December 31, 2011

Allegation 3 (a) he failed to carry out sufficient appropriate analytical procedures to support the plausibility of information contained in the financial statements.

41. The financial statements Doc pp. 65-77 are with respect to a family farm with gross revenues of \$2.2 million and retained earnings of \$3 million. Revenue is generated from grain, cattle and tilling of fields for irrigation purposes.
42. Although the planning section of the file contains a working paper with ratios calculated by the AFP system working paper software Doc pp. 78-79, there is no evidence that work was performed on the results. In order to comply with standards for a review engagement (CICA 8100.15 (iii) (a), 8100.19 (b)) **Tab 1**, analysis of these ratios is a primary form of evidence.
43. The member has failed to carry out sufficient appropriate analytical procedures to satisfy himself that the income statement items are plausible.
44. Once Shanks was satisfied with the balance sheet he improperly assumed the income statement was correct.
45. Insufficient work was done to ensure the income statement was plausible.

Allegation 3 (b) he failed to assess materiality.

46. A materiality worksheet is included in the working paper file Doc pp. 80-81. This worksheet is not filled in and Shanks did not set an amount as materiality. CICA Handbook s. 8100.22 **Tab 1** requires a member reviewing financial statements to make a determination with respect to materiality.

Allegation 3 (c) he failed to document matters important to support the review engagement report.

47. Generally accepted standards of practice require the member carrying out a review to document matters important to support the review engagement report (CICA 8100.15 review standards, 8100.19-22 review procedures). **Tab 1**
48. Shanks did not document the analysis he performed on ratios calculated by the AFP system.
49. Loan agreements supporting the long term debt of \$2.72 million Doc p. 68 were not documented in the permanent file.
50. There was inadequate documentation of inquiry and discussions that Shanks said he had with the client particularly with respect to income statement accounts.

Terms of Settlement

51. Shanks and the Professional Conduct Committee agree to the following Terms of Settlement:
- a) Shanks hereby tenders his resignation pursuant to Bylaw 4.18.1 along with his certificate of membership as a Chartered Accountant and his certificate of membership as a Chartered Professional Accountant and his Licence to Practice as a Public Accountant in the Province of Ontario and consents to the Discipline Committee making an order, pursuant to Regulation 7-3 section 10.14 that his resignation be effective immediately.
 - b) By signing this Settlement Agreement Shanks undertakes not to apply for membership in the Institute, or for a Public Accounting Licence, in the future;
 - c) Shanks will pay costs in the amount of \$10,000 within three months of this agreement receiving approval of the Discipline Committee;
 - d) Notice of the terms of this Settlement Agreement will be given in accordance with ICAO Regulation 7-3, sections 22- 23 including to the Public Accountants' Council, the CICA, in *Checkmark Magazine* and in the local newspaper, the *Tilbury Times*, with costs of publication in the *Tilbury Times* to be borne by Shanks.
52. Should the Discipline Committee accept this Settlement Agreement, Shanks agrees to waive his right to a full hearing, judicial review or appeal of the matter subject to the Settlement Agreement. The allegations approved by the Professional Conduct Committee and attached to this agreement shall be stayed.

If Settlement Agreement Not Approved

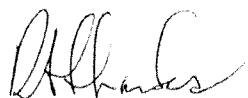
53. If, for any reason, this Settlement Agreement is not approved by the Discipline Committee, then;
- a) This Settlement Agreement and its terms, including all settlement negotiations between the Professional Conduct Committee and Shanks leading up to its

presentation to the Discipline Committee, shall be without prejudice to the Professional Conduct Committee and Shanks;

- b) The Professional Conduct Committee and Shanks shall be entitled to all available proceedings, remedies and challenges, including proceeding to a hearing on the merits of the allegations, or negotiating a new Settlement Agreement, unaffected by this Settlement Agreement or the settlement negotiations;
- c) The terms of this Settlement Agreement will not be referred to in any subsequent proceeding, or disclosed to any person, except with the written consent of the Professional Conduct Committee and Shanks or as may be required by law.

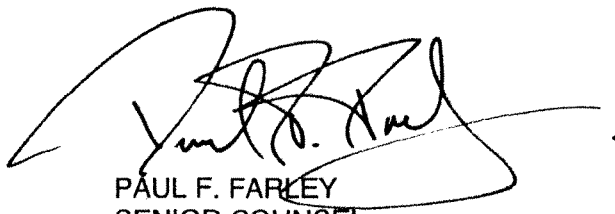
54. Any obligations of confidentiality shall terminate upon approval of the Settlement Agreement by the Discipline Committee.

All of which is agreed to for the purpose of this proceeding alone this 13th day of March, 2013.



ROBERT A. SHANKS, CPA, CA

On his own behalf



PAUL F. FARLEY
SENIOR COUNSEL,
PROFESSIONAL CONDUCT COMMITTEE
On behalf of the Committee