



# THE INSTITUTE OF CHARTERED ACCOUNTANTS OF ONTARIO

DISCIPLINE COMMITTEE - CHAIR  
MURRAY FINKELMAN

EL 1 NOVEMBER 8, 2010  
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**IN THE MATTER OF:** CHARGES AGAINST MURRAY A.  
FINKELMAN, CA, A MEMBER OF THE  
INSTITUTE, BEFORE THE DISCIPLINE  
COMMITTEE

## SETTLEMENT AGREEMENT

*made pursuant to Bylaw 510 (7.1) of the Bylaws of the  
Institute of Chartered Accountants of Ontario*

### Introduction

1. The Professional Conduct Committee ("PCC"), at their meeting of February 9, 2010, approved draft charges against Murray A. Finkelman, CA ("Finkelman") Charges were signed by the Deputy Chair on March 31, 2010 (Schedule 1).
2. The charges pertain to professional work done by Finkelman with respect to the audit of financial statements of PLC Limited for the years ended October 31, 2005 (page 1) and October 31, 2006 (page 10).
3. The charges also pertain to professional work done by Finkelman with respect to a report dated December 10, 2005, wherein he reviewed the purchase by his client, PLC Limited, of lumber from LL Limited (page 19).
4. The Professional Conduct Committee and Finkelman agree with the facts and conclusions set out in this settlement agreement for the purpose of this proceeding and this proceeding only.

### **Member Background**

5. Finkelman obtained his CA designation in 1957. He was employed by Norman Solomon, CA up to 1994. Since that time he has been a sole practitioner.
6. Finkelman's current practice consists of 6-7 review engagements and 30-40 compilation engagements as well as a limited number of personal tax returns.
7. PLC has been a client of Finkelman's for approximately 40 years. The company is a family owned finished lumber business headed by Bernard N ("Bernard"). Finkelman was engaged to audit the financial statements of PLC for the years ended October 31, 2005 (page 1) and 2006 (page 10).
8. Finkelman has done no audits since the audit of PLC described in the charges. He does not employ staff and works out of a single room office with a shared reception area in North Toronto. He is a member of the Canadian Tax Foundation and the Canadian Public Accountability Board (CPAB). Finkelman expects to retire within the next two years and is in the process of resigning from CPAB.

### **Charge 1 – Audit of PLC Financial Statements - October 31, 2005 (DOC 1)**

9. The audit of PLC for the October 31, 2005 year end was carried out by Finkelman. He did not employ staff on the audit but did all of the work himself. The audit report (page 3) was signed by Finkelman and released. The copy of the financial statements at (page 1-9) is a file copy of the financial statements released.
10. It is agreed that in carrying out his audit Finkelman failed to perform his professional services in accordance with generally accepted standards of practice of the profession including the recommendations set out in the *CICA Handbook* referenced below. In particular Finkelman failed:

#### ***(a) to obtain a representation letter dated the same date as the Auditor's Report;***

11. The representation letter (page 26) was dated January 16, 2006 prior to the date on the auditor's report of January 18 (page 3). This is a failure to comply with the *CICA Handbook*. (5370.23 *CICA Handbook* page 58).

**(b) to obtain legal confirmation letters;**

12. A legal confirmation letter was not obtained as required by the Handbook. (6560.07 CICA Handbook page 63)

**(c) to assess compliance with the independence requirements applicable to the engagement;**

13. PLC had been an audit client for approximately 40 years, but Finkelman did not consider the effect that his familiarity with the client had on his independence.
14. In addition to auditing the financial statements of PLC during the relevant period Finkelman performed accounting services for PLC including monitoring the company's cash flows and comparing the details of unsigned cheques to supporting documents prior to Bernard signing the cheques. Finkelman did not consider the effect that these services had on his independence.
15. Finkelman's total fees for 2005 and 2006 were \$179,000 and \$165,000 respectively. His fees from PLC totaled 13.4% of the 2005 fees and 14.5% of the 2006 fees. Because of the significance of the fees charged to PLC as a % of his total practice fees Finkelman should have turned his mind to the issue of independence. He did not do so. (5030.15 CICA Handbook page 33)

**(d) to properly assess the components of audit risk;**

16. While Finkelman recognized that high risk areas of the audit were inventory and payables he did not document his assessment of these risks in particular and he did not assess the components of audit risk in general at the planning stage. (6560.07 CICA Handbook page 63)

**(e) to assess Control Risk or test internal controls;**

17. There was no assessment of control risk and no testing of internal controls. (5210.33, 5210.14 CICA Handbook page 50)

**(f) to obtain sufficient appropriate audit evidence with respect to valuation of the balance sheet item "Inventory (Note 1(b)) 3,763,532" and support for an inventory write-down of \$70,000;**

18. Finkelman attended at the inventory count, performed mechanical calculations in respect of the overhead allocations and looked at sales subsequent to year end; however, he obtained insufficient evidence with respect to inventory value.
19. Inventory value was based on his knowledge of what the client had paid during the year. He relied primarily on management's representations about overhead allocation rates.
20. Work was not performed to substantiate the quality of the lumber beyond observing some inventory that he knew had been stained. Analytical review procedures and cut-off tests were not done. All of these steps were insufficient audit evidence to enable the auditor to provide an opinion on the fair presentation of inventory on the financial statements. (6030 *CICA Handbook* page 60)
21. Inventory had been written down by \$70,000 (with an offsetting reduction in accrued charges) in respect of the inventory acquired from LL Limited on the basis that the grade and quality of the inventory was less than what had been paid for. While Finkelman did see email correspondence from LL Limited offering a \$63,000 credit to settle the dispute he did not have the email documented in his file and there was no evidence of acceptance of that settlement offer by PLC. This was not sufficient audit evidence supporting the write-down. (6030 of the *CICA Handbook* page 60)
22. Finkelman knew that there were major issues pertaining to the staining of lumber inventory which could significantly affect the value of inventory. In carrying out his audit Finkelman observed some staining at the inventory count, but relied solely on the representations of PLC about the extent of the staining and made no enquiries during the audit as to the steps being taken to prevent further spread of the staining so as to assess whether the inventory could be saleable in the future (6030 *CICA Handbook* page 60).

**(g) with respect to financial instruments, to ensure disclosure in the notes to the financial statements, of risk and fair value and the carrying value of advances from shareholders;**

23. Note 1(f) to the financial statements (page 8) refers to financial instruments.

Finkelman failed to ensure disclosure in the notes to the financial statements of the risk and fair value of financial instruments. In addition the fair value of shareholders advances Note 5 (page 9) was not disclosed. (3860 CICA Handbook page 13)

**(h) to ensure disclosure of the details with respect to balances with related parties;**

24. The note 2 to the financial statements disclosed that there was an accounts receivable balance from a related company (page 8), however, Finkelman failed to disclose the nature of the relationship with the related party as required. (3840 CICA Handbook page 8)

**(i) to ensure disclosure of the company accounting policy with respect to income taxes;**

25. In Note 1 to the financial statements "Accounting Policies" (page 8) Finkelman failed to disclose the accounting policy with respect to income taxes. (3465 CICA Handbook page 6)

**(j) to ensure proper disclosure of the details surrounding "Bank loan-operating (Note 4) 2,619,000" including terms and interest rate;**

26. In Note 4 "Bank Loans" (page 9) Finkelman failed to ensure proper disclosure of the terms and conditions of the operating bank loan in the amount of \$2,619,000, including interest rate (3860.52 CICA Handbook page 13) and the effective interest rate (3860.57 CICA Handbook page 13).

**(k) to document evidence required to support the Auditor's Report**

27. With respect to the audit work done on inventory Finkelman failed to document:

- a) Finkelman's understanding of internal control (5205.13 CICA Handbook page 48).

- b) The basis for determining the sample selected at the inventory count.
- c) Work performed in respect of inventory valuation (5025.53 CICA Handbook page 30).

28. In addition Finkelman failed to document his understanding of PLC's internal control for purposes of planning the audit.

29. Finkelman reviewed November and December sales to assess net realizable value of inventory; however, he did not document the work performed in his working paper file.

30. With respect to audit work performed relating to the \$70,000 write down in inventory obtained from LL Limited Finkelman did review email correspondence between LL Limited and PLC but he did not document this evidence in his working paper file.

31. It is agreed that with respect to the audit of the financial statements of PLC Limited for the year ended October 31, 2005 Finkelman failed to perform his professional services in accordance with generally accepted standards of practice of the profession.

### **Charge 2 – Audit of PLC for October 31, 2006**

32. The audit of PLC for the October 31, 2006 year end was carried out by Finkelman. He did not employ staff on the audit but did all of the work himself. The audit report was signed by Finkelman and released. The copy at (page 10-18) is a file copy of the released report and financial statements

33. In carrying out his audit Finkelman failed to perform his professional services in accordance with generally accepted standards of practice of the profession including the recommendations set out in the CICA Handbook referenced below. In particular Finkelman failed:

#### ***(a) to obtain legal confirmations;***

34. A legal confirmation letter was not obtained. (6560.07 CICA Handbook page 63)

***(b) To assess compliance with the independence requirements applicable to the engagement;***

35. Finkelman did not document the nature of his relationship with the client. PLC had been an audit client of Finkelman's for approximately 40 years, but he did not consider the effect that his familiarity with the client had on his independence.
36. Finkelman performed services for PLC including monitoring the company's cash flows and comparing the details of unsigned cheques to supporting documents prior to Bernard signing the cheque. Finkelman did not consider the effect that these services had on his independence.
37. Finkelman's total fees for 2005 and 2006 were \$179,000 and \$165,000 respectively. His fees from PLC totaled 13.4% of the 2005 fees and 14.5% of the 2006 fees. Because of the significance of the fees charged to PLC as a % of his total practice fees Finkelman should have turned his mind to the issue of independence. He did not do so. (5030.15 CICA Handbook page 33)

***(c) to carry out preliminary analytics at the planning stage;***

38. Finkelman did not perform, at the planning stage, preliminary analytics. (5141.07 CICA Handbook page 39)

***(d) to properly assess risk by financial statement area and to document an overall audit response to risk;***

39. Finkelman did not carry out risk assessment by financial statement area. (5143.02 CICA Handbook page 42)
40. There was no documentation of the overall response to audit risk. In particular Finkelman did not review:
  - a) *the overall audit responses to address the assessed risks of material misstatement at the financial statement level and the nature, timing and extent of the further audit procedures;*

(b) *the linkage of those procedures with the assessed risks at the assertion level.*  
(5143.75 CICA Handbook page 42)

**(e) to obtain sufficient appropriate audit evidence with respect to valuation of the balance sheet item "Inventory (Note 1(b) 3,088,816";**

41. In 2006, the remaining amount of stained or defective inventory from LL was written off, with a corresponding reduction in Accounts Payable. There is no reference in the Note 1(b) (page 16) to the write-off.
42. Finkelman indicated that he did review email evidencing the intention of PLC to make no payment with respect to the inventory written off but there was no evidence in the working paper file.
43. With respect to valuing the inventory written off Finkelman only viewed the inventory that the client said was segregated in the yard and concluded from his viewing that the value assigned appeared reasonable. No confirmation was obtained from LL Limited as to the balance written off and no written representation from management was obtained.
44. It is agreed that Finkelman did not obtain sufficient appropriate audit evidence to support the inventory amount shown on the balance sheet (page 12). (6030 CICA Handbook page 60)

**(f) with respect to financial instruments, to ensure disclosure in the notes to the financial statements, of risk and fair value and the carrying value of advances from shareholders;**

45. While Finkelman referred to financial instruments in Note 1(f) (page 16) he failed to ensure disclosure of the risk and fair value of financial instruments. In addition the fair value of shareholder advances was not disclosed in Note 5 (page 17). (3860 CICA Handbook page 13)



***(g) to ensure disclosure of the details with respect to balances with related parties;***

46. The notes to the financial statements disclosed that there was an accounts receivable balance from a related party (page 16), however, Finkelman failed to disclose details of the nature of the relationship with the related party . (3840 *CICA Handbook* page 8)

***(h) to ensure disclosure of the company accounting policy with respect to income taxes;***

47. Finkelman failed to disclose the accounting policy with respect to income taxes (page 16). (3465 *CICA Handbook* page 6)

***(i) to ensure proper disclosure of the details surrounding "Bank Loans (Note 4) 1,609,000" including terms and interest rate;***

48. Finkelman failed to ensure disclosure in Note 4 "Bank Loans" (page 17) of the terms and conditions of the operating bank loan in the amount of \$1,609,000, including interest rate (3860.52 of the *CICA Handbook*) and the effective interest rate (3860.57 of the *CICA Handbook* page 13).

***(j) to ensure proper disclosure of the terms, interest rate and payments over the following five years of "Long-term Liabilities Bank Term Loan (Note 4) 625,000";***

49. Finkelman failed to ensure disclosure in Note 4 (page 17) of the terms and conditions of the long term liabilities (3860.52 *CICA Handbook* page 13), the effective interest rate of the long term liabilities (3860.57 *CICA Handbook* page 13) and the payments over the next five years (3210.03 *CICA Handbook* page 1)

***(k) to ensure proper disclosure in the notes to the financial statements of contingent liabilities;***

50. Note 7 to the financial statements (page 18) disclosed that the company was disputing the balance claimed by a supplier. However Finkelman did not disclose an estimate of the amount of the contingent loss or note that such an estimate cannot be made. (3290.22 CICA Handbook page 3)

***(l) to document evidence required to support the Auditor's Report.***

51. Finkelman's failure to document audit evidence to support the audit report is referred to in the paragraphs above.

52. In particular there is no documentation in the working paper file in respect of the valuation of the inventory or the appropriateness of reversing the accounts payable balance.

53. There is no documentation with respect to independence considerations and an independence letter is not in the file.

54. There was no documentation relating to assessment of risks by financial statement area.

55. There is no documentation of testing of internal controls.

56. It is agreed that with respect to the audit of the financial statements of PLC Limited for the year ended October 31, 2006 Finkelman failed to perform his professional services in accordance with generally accepted standards of practice of the profession.

### **Charge 3 – Rule 204.1**

57. During the relevant time period, in addition to auditing the financial statements of PLC Finkelman reviewed the payables bi-monthly ensuring proper approvals and delivery of goods.

58. Finkelman monitored the cash flow of PLC. If he determined that the company's credit limit may be exceeded, he requested the bookkeeper to withhold the cheque. In other instances, he told the bookkeeper to take advantage of an early payment discount. He reviewed schedules prepared by staff before they go to the bank.
59. Twice a month, Finkelman reviewed the PLC cheque listing, unsigned cheques and supporting documents such as invoices and purchase orders to ensure there were proper staff approval signatures, that the pricing is correct, the appropriate chargebacks/deductions are made and that the goods delivered are within the parameters of the purchase order. He questioned an invoice if he considered the pricing to be too high. Once his review was complete, he signed on the cheque listing and the package was sent to Bernard for signing.
60. Finkelman reviewed all accounting schedules prepared by PLC staff before they were forwarded to the bank.
61. Finkelman prepared annual corporate tax returns for PLC.
62. Finkelman prepared Notice to Reader statements, corporate or personal tax returns for:
- Bernard's law practice
  - Bernard's family company that owns 71 rental apartments
  - Several other small companies belonging to Bernard
  - Bernard's sister in law.
63. It is agreed that in carrying out this work for PLC and related parties during the period he was engaged to audit the financial statements of the company Finkelman made management decisions and performed management functions for the company and therefore failed to remain independent in performing his audits of the financial statements of PLC for the years ended October 2005 and 2006 contrary to Rule 204.1 of the Rules of Professional Conduct.

#### **Charge 4 - Background**

64. LL Limited is in the business of logging and production of lumber. PLC was a new customer of LL Limited.
65. LL Limited sold to PLC a large quantity of lumber (2.7 million FBM "feet board measure") in April 2005 through P.O. # 280 (page 22). Feet board measure represents a board 24 x 6 x 1 inches.
66. The lumber was delivered in May through October 2006 and a dispute arose with regard to whether the lumber price should be discounted because of inferior quality (Grade) and staining of the wood.
67. Finkelman was asked by Bernard to prepare a report in support of his position that the lumber delivered through PO #280 (page 22) was inferior.
68. Finkelman prepared a report (page 19-21) ("report") which he understood to be restricted to Bernard's own use in his negotiations with LL Limited regarding amounts owing on PO #280.
69. Finkelman had nothing in writing from PLC regarding the engagement and there was no engagement letter. Because Finkelman believed that this was a review engagement he should have complied with the *CICA Handbook* sections 8100 General Review Standards and 8500 Reviews of Financial Information Other than Financial Statements.
70. Section 8100.11 (*CICA Handbook* page 67) states:
 

*'there should be a clear understanding and agreement between the public accountant and the client as to the nature and terms of a review engagement and it is highly desirable that such agreement be in writing to avoid misunderstandings'.*
71. In this case there was not a clear understanding of the nature and terms of the engagement.

72. Bernard forwarded Finkelman's report to LL Limited on December 12, 2005 with a cheque for the outstanding balance on PO #280 as supported by Finkelman's report.
73. The report was described by Bernard as a 'Reconciliation Report' and provided an account of amounts paid to date on PO #280 with calculations by Finkelman of charge backs to be deducted from the final payment as a result of quality issues.
74. LL Limited responded to PLC on December 13, 2005 and accepted the grade and shortage amounts in the report but challenged the stain percentage.
75. LL Limited accepted the reductions in the report relying on the fact that Finkelman was a CA. It is agreed that the report was used in negotiations between the supplier and customer.

**Charge 4 (a)**

76. Although Finkelman believed he was carrying out a review engagement he did not include a paragraph in his report setting out the scope and the restrictions on use of his report as required. (section 8100.26 & .44 *CICA Handbook* page 67)

**Charge 4 (b),(c)**

77. In preparing his report, Finkelman relied on schedules prepared by PLC staff and he relied on the PLC staff count and their assessment on quality recorded on the tally cards.
78. Finkelman did visit the lumberyard and meet with PLC staff to view the stained lumber but no formal quantification was made by him.
79. The lumber described in P.O. #280 (page 22) was produced in two batches (first and second cut) and delivered in 46 and 76 loads respectively. Finkelman examined supporting documents relating to 31 loads from the second cut only.
80. At the time of his review on November 8, 2005, the first cut had not been checked for grade quality and only 31 loads from the second batch had been checked by the client.

81. In his December 10, 2005 report (page 19) Finkelman states *'I have reviewed all supporting documents, including tallies, grade out reports, invoices and purchase orders....'*
82. His summary refers to " Stained Lumber 25% actual" (page 21)
83. Finkelman did not carry out the review he said was carried out and the amounts should not have been described as "actual" (page 21) since they were estimates of PLC management based on assumptions. His report implied that a full and thorough investigation had been performed and that the information was complete when it was not.
84. In fact the review carried out by Finkelman was of a box of documents sent to him by PLC. Finkelman's review of supporting documents represented only 24.5% of the total delivery related to PO #280.
85. The numbers in Finkelman's report (page 19-21) primarily come from two schedules prepared by PLC staff:
- *Schedule dated November 21, 2005 ("Tally Schedule")* - this schedule provides a breakdown by invoice number of shipments, actual tallies, stained count and amounts paid to date (page 23).
  - *Schedule dated November 9, 2005 ("Grade Schedule")* - this schedule provides a listing of loads graded and grade levels (page 24).
86. The underlying documentation reviewed by Finkelman to verify the amounts on the above schedules regarding the second shipment include the following:
1. LL Limited Invoices
  2. Bills of Lading
  3. A selection of some of the Tally cards that were prepared for each load. These cards indicate counts relating to stain and below grade quantities

87. Finkelman did not review any documentation relating to the first cut. With respect to the second cut he was not sent every tally card and of the tally cards he did receive, he did not check every item on the card to the Tally Schedule.
88. Finkelman reported "*Stained lumber 25% 'actual'*" (page 21). The Tally schedule reviewed by Mr. Finkelman (Page 23) indicated a stain percentage of 1.17% ( $30,130/2,577,433$ ). Finkelman, however, prepared his calculations using 25% (being 15% over the 10% allowance per the PO) based on Bernard's request to make that assumption. In Bernard's email of October 14, 2005, he requested 'for now, calculate 15% adjustment' (page 25). In addition the percentage was based on 30 loads inspected by the client out of a total of 122 and not 'actual'.

#### **Charge 4(d)**

89. Finkelman reported "*Amount Received below Grade – 53.79 actual*" (page 21). The source of this percentage number comes from the Grade Schedule (page 24) prepared by the client that Finkelman reviewed. According to the schedule, the percentage below grade was based on 31 loads inspected by the client out of a total of 122 loads and not 'actual'.
90. The reference to 'actual' per Finkelman's reporting letter (page 21) implied that all 122 loads were inspected and graded by the client when they were not.
91. It is agreed that Finkelman, in preparing his report dated December 10, 2005, failed to exercise due care.

#### **Terms of Settlement**

92. Finkelman and the Professional Conduct Committee agree to the following Terms of Settlement:
- a) Finkelman will be reprimanded by the Chair of the Discipline Committee in writing;
  - b) Finkelman will make a payment by way of fine in the amount of \$8,000;
  - c) Finkelman will take, within eighteen months, <sup>four</sup> ~~three~~ professional development courses including: <sub>of U</sub>

- (i) Review Engagements;
  - (ii) Audit & Review Engagements – Required Communications;
  - (iii) Professional Risk Management – A Practical Perspective, and
  - (iv) Effective Use of Analytical Procedures.
- d) Finkelman undertakes not to act as engagement partner on any audit;
- e) Finkelman will engage a Supervisor approved by the Director of Standards Enforcement who will review all Review Engagements carried out by Finkelman for a period of eighteen months from the date this Settlement Agreement is approved by the Discipline committee and no Review Report will be released by Finkelman without the prior approval of the Supervisor;
- f) Finkelman will have his Review Engagement practice reinvestigated by the Professional Conduct Committee following the period of supervision with costs of the reinvestigation up to \$2,000 to be borne by Finkelman.
- g) There will be full publicity in CheckMark Magazine of this Settlement;
- h) Finkelman will be allowed three months from the time the Discipline Committee accepts this Settlement Agreement to pay the costs and fines referred to herein.
93. Should the Discipline Committee accept this Settlement Agreement, Finkelman agrees to waive his right to a full hearing, judicial review or appeal of the matter subject to the settlement agreement. The charges approved by the Professional Conduct Committee and dated March 31, 2010 shall be forever stayed.
94. 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 Finkelman leading up to its presentation to the Discipline Committee, shall be without prejudice to the Professional Conduct Committee and Finkelman;
  - b) The Professional Conduct Committee and Finkelman shall be entitled to all available proceedings, remedies and challenges, including proceeding to a



hearing on the merits of the allegations set out in the charges, or negotiating a new Settlement Agreement, unaffected by this Settlement Agreement or the Settlement Negotiations;

**Disclosure of Settlement Agreement**

95. This Settlement Agreement and its terms will be treated as confidential by the Professional Conduct Committee and Finkelman, until approved by the Discipline Committee, and forever if, for any reason whatsoever, this Settlement Agreement is not approved by the Discipline Committee, except with the written consent of the Professional Conduct Committee and Finkelman, or, as may be required by law.

96. 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 28<sup>th</sup> day of October 2010.



PAUL F. FARLEY  
SENIOR COUNSEL

On behalf of;  
THE PROFESSIONAL CONDUCT COMMITTEE



MURRAY A. FINKELMAN, CA  
on his own behalf