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• Please refer the CPE & Support Handout in the Handouts section for more information about group participation and CPE certificates.

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LEARNING OBJECTIVES

- Recognize the auditor and audit committee requirements with respect to addressing illegal acts under Section 10A of the SEC Exchange Act
- Describe the roles of the board, management, counsel, and the auditor with respect to identification and potential remediation of illegal acts
- Identify the steps involved in an investigation of an illegal act and assess the adequacy of your company's policies/procedures with respect to such

RESPONDING TO ILLEGAL ACTS: AUTHORITATIVE LITERATURE, ROLES, & RESPONSIBILITIES
ILLEGAL ACTS AND NONCOMPLIANCE

• Authoritative Literature
  • PCAOB AU Section 317, Illegal Acts by Clients*
  • AICPA AU-C 250, Consideration of Laws and Regulations in an Audit of Financial Statements*

  *Requirements and guidance are similar in both standards

• SEC Section 10A of the 1934 Act

DEFINITIONS

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<td>Violations of laws or government regulations. Illegal acts by clients are acts attributable to the entity whose financial statements are under audit or acts by management or employees acting on behalf of the entity. Illegal acts by clients do not include personal misconduct by the entity’s personnel unrelated to their business activities.</td>
<td>Acts of omission or commission by the entity, either intentional or unintentional, which are contrary to the prevailing laws or regulations. Such acts include transactions entered into by, or in the name of, the entity or on its behalf by those charged with governance, management, or employees. Noncompliance does not include personal misconduct (unrelated to the business activities of the entity) by those charged with governance, management, or employees of the entity.</td>
<td>Acts or omissions that violate any law, or any rule or regulation having the force of law.</td>
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ILLEGAL ACT BASICS - AUDITOR’S PERSPECTIVE
RELATIONSHIP TO FINANCIAL STATEMENTS

• Direct and Material Effect
  • Auditors consider laws and regulations that are generally recognized to have a direct and material effect on the financial statement amounts
    • For example, tax and pension laws and regulations
  • Auditor’s responsibility to detect and report these illegal acts is the same as that for misstatements caused by error or fraud

• Indirect Effect
  • Laws or regulations that relate more to operational aspects
  • Even when violations of indirect laws/regs may be material to the financial statements, the auditor may not become aware of such unless informed by client or there is other information as a result of other audit procedures
  • An audit provides no assurance that illegal acts will be detected or contingent liabilities that result will be disclosed

ILLEGAL ACT BASICS - AUDITOR’S PERSPECTIVE

• Audit Procedures when noncompliance is identified or suspected:
  • Obtain an understanding of the nature of the act and circumstances in which it occurred and sufficient further information to evaluate effect on F/S
    • Inquire of management at a level above those involved
    • Specific procedures to consider if management does not respond satisfactorily
  • Consider implications in relation to risk assessment and written representations and effect on F/S
  • Consider effects on F/S and whether to consult with legal counsel
    • Is the impact material?
SECTION 10A OF SECURITIES EXCHANGE ACT OF 1934:
AUDITOR’S RESPONSIBILITIES

Step 1
- Ensure AC Chair is informed
- Inform appropriate level of management

Step 2
- Determine whether it is likely that an illegal act has occurred

Step 3
- Determine and consider possible effects of the illegal act on the F/S

Step 4
- Determine whether management has taken timely and appropriate remedial action with respect to the illegal act

Step 5
- If management has failed to take remedial action, evaluate need for a departure from standard audit report or resignation

Step 6
- Determine whether to report to the Board

SECTION 10A OF SECURITIES EXCHANGE ACT OF 1934:
BOARD’S RESPONSIBILITY

When Will A Report to the SEC Be Necessary?

- If the issuer’s management does not satisfactorily address these questions, then the auditor must report that failure to the Board, and the Board must report to the SEC (and the auditor must report to the SEC if the Board does not).
  - One business day!

- If the issuer’s management does satisfactorily address these questions, then no reporting is necessary.
OVERVIEW OF THE INVESTIGATION PROCESS

INVESTIGATORY PROCESS

- Determine the scope
- Use of internal and external resources
- Implement remedial measures
- Determine exposure
- Maintain privilege
- Oversight of the investigation
Who does the determination as to whether the alleged act is illegal?
How does the auditor determine the impact on the financial statements?

Can the external auditor determine the scope of the investigation?
What should the auditor do if he/she has concerns about the scope/nature of the investigation?

When should counsel be engaged to investigate potential misconduct? When does the Board (versus management) need to engage counsel and manage the investigation?
Outside of regulatory exposure, what other exposure is there when a company is conducting an internal investigation?

Why should the investigation be independent?
How does the attorney-client privilege work in the context of an investigation? What is privileged? What is not? How do you keep external stakeholders (regulators, auditors, etc.) informed while preserving privilege?

How should the auditor engage with or communicate with management during the investigation?
How does the shadow investigation differ from the independent investigation being performed?

How much time does the shadow investigation take?
What have you seen a board or directors do that may have hindered the internal investigation and its effectiveness?

How does the recent Yates memorandum affect internal investigations and what should a board know about the memorandum?
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BDO BOARD GOVERNANCE - WEBINARS

Upcoming Webinars:
• The New Lease Accounting Standard - May 12, 2016
• M&A Execution: Planning with Post-Integration in Mind - May 26, 2016

Recent Archived Webinars:
• Board Diagnostics and Enhancing Your Governance Practices - April 2016
• Quarterly Technical Update (Q1 2016) - April 2016
• Managing Risk: Elevation of Cybersecurity to the Boardroom - February 2016
• The Board’s Role in Emerging Practices in Risk Management - January 2016
• What’s On the Minds of Boards - January 2016
• Quarterly Technical Update (Q4 2015) - January 2016
• Effective Audit Committees - November 2015
• Establishing an Effective Internal Audit Function - October 2015
• The Board’s Role in Anticorruption Compliance - October 2015

BDO BOARD GOVERNANCE - PUBLICATIONS

Additional resources accessible via BDO Board Governance:
https://www.bdo.com/services/assurance/board-governance/overview
• BDO Shareholder Meeting Alert 2016
• Fatal Flaws in Fraud Risk Management
• Elevating Cybersecurity to the Board - Questions Boards Should Be Asking
• FASB Issues ASU on Leases
• 9 Questions Organizations Should Ask About Risk Management
• BDO 600 2015 Survey of Directors Compensation Practices
• 2016 BDO Tax Outlook Survey
• Managing and Preventing Tax-Related Identity Theft
• 2016 BDO IPO Outlook
• BDO 600 2015 Survey of CEO and CFO Compensation Practices
• PCAOB Adopts rules Requiring Disclosure of the Engagement Partner...
• Proxy Voting Policies Focus on Overboarding
• CAQ Issues 2015 Audit Committee Transparency Barometer
• 2015 Board Survey

For a complete listing of BDO publications, refer to: https://www.bdo.com/insights/
EVALUATION

We continually try and improve our programming and appreciate constructive feedback.

Following the program, we will be sending out a thank you e-mail that contains a link to a brief evaluation.

Thank you in advance for your participation!

CONCLUSION
THANK YOU FOR YOUR PARTICIPATION!

Certificate Availability - If you participated the entire time and responded to at least 75% of the polling questions, click the Participation tab to access the print certificate button.

Please exit the interface by clicking the red “X” in the upper right hand corner of your screen.
TIM CLACKETT, CPA
Assurance Partner

EXPERIENCE SUMMARY
Tim has more than 29 years of accounting experience and has worked in both public accounting and in industry as a corporate vice president and controller. He has worked with a wide variety of national and international public and private corporate clients and has significant experience advising companies in the manufacturing and distribution, cleantech, services, entertainment, and biotechnology industries. He has assisted clients with initial public offerings, secondary offerings and other debt and equity placements.

Tim heads the firm’s cleantech initiative for the western region and frequently is involved in industry conferences and seminars and writing thought pieces.

PROFESSIONAL AFFILIATIONS
• Association of Chartered Accountants in the United States
• British American Business Council
• California Society of Certified Public Accountants
• The Institute of Chartered Accountants in England & Wales

EDUCATION
• B.A., Economics/Economic History, University of Leicester, United Kingdom

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KEN GEE, CPA
National Assurance Partner

EXPERIENCE SUMMARY
Ken is a partner in the National Assurance Practice of BDO USA, LLP. In this role, he advises clients on accounting for complex transactions with a focus on revenue recognition, business combinations, and stock-based compensation. Ken is also a member of BDO’s National Assurance Committee, which establishes the Firm’s internal policies.

Ken authors and presents technical training courses on financial accounting and reporting developments within BDO and for external audiences.

Previously, Ken was a client service partner in BDO’s Technology and Life Science Practice and served both public and private companies.

PROFESSIONAL AFFILIATIONS
• American Institute of Certified Public Accountants
• California Society of Certified Public Accountants

EDUCATION
• B.B.A., Accounting, University of Notre Dame

A. JOSEPH JAY III
Special Counsel
Cadwalader, Wickersham & Taft, LLP

EXPERIENCE SUMMARY
Joseph Jay represents corporations and individuals in criminal and regulatory matters before the U.S. Department of Justice, the SEC, Federal Inspectors General, and U.S. Attorneys’ Offices. Recent matters have included allegations of violations of the FCPA, securities and accounting fraud, antitrust, export controls, and conflicts-of-interest, bribery, and unlawful gratuities.

Joe counsels clients regarding organizational compliance programs and procedures. Joe has designed, developed, implemented, and tested global compliance programs tailored to individualized risk-based assessments, inclusive of anticorruption programs and compliance with Sarbanes-Oxley, OFAC and AML regulations.

Joe has conducted numerous internal investigations involving a broad range of alleged or suspected misconduct and regularly represents Boards of Directors, Audit Committees, and other companies in complex independent and internal investigations around the world. He has broad experience in matters involving the World Bank and other multi-lateral development organizations.

EDUCATION
• J.D., William & Mary School of Law
• College of William & Mary
EXPERIENCE SUMMARY

Adria Perez focuses her practice on representing both corporations and individuals in white collar criminal defense matters, government enforcement issues, as well as internal, criminal and SEC investigations. Her experience includes handling issues relating to the Foreign Corrupt Practices Act, False Claims Act (including government contracting, healthcare and tax matters), Civil Investigative Demands and export enforcement. Ms. Perez assists clients in responding to inquiries from and government investigations conducted by the DOJ, SEC, OCC and Office of Inspector General from a variety of federal agencies. She also counsels clients on developing and strengthening compliance programs and policies.

PROFESSIONAL AFFILIATIONS

- American Bar Association
- Hispanic National Bar Association

EDUCATION

- Columbia University, J.D.
- Florida State University, B.A., International Affairs and Spanish, summa cum laude
- Parker School of International Law, Certificate in Comparative and International Law

MARYELLEN SEBOLD, CPA
Managing Director

EXPERIENCE SUMMARY

Maryellen Sebold is a Managing Director in the Dispute Advisory Services practice of BDO Consulting in Los Angeles. With more than 28 years of experience in the areas of forensic accounting and fraud investigations, litigation consulting, bankruptcy and corporate restructuring, Ms. Sebold brings her specialized knowledge to her cases, applying such expertise to a broad spectrum of issues. She is frequently hired as an expert witness to testify as to economic damages, lost profits, alter-ego and tracing of assets. In addition, she conducts internal investigations into allegations of fraud and mismanagement and conducts operational assessments of businesses struggling with underperformance issues.

Ms. Sebold has experience in a wide range of industries, including healthcare, manufacturing, construction, entertainment, franchises, insurance, publishing, real estate, securities and transportation. She is a Certified Public Accountant, Certified Insolvency and Restructuring Advisor and is Certified in Financial Forensics. Ms. Sebold is currently on the Board of CalCPA, is on the AICPA Council and is a Past-President of the CalCPA Education Foundation.

PROFESSIONAL AFFILIATIONS

- CalCPA Board member
- AICPA Council member
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