

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 92378 / July 13, 2021**

**ACCOUNTING AND AUDITING ENFORCEMENT**  
**Release No. 4225 / July 13, 2021**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-20394**

**In the Matter of**

**PAUL L. CHANCEY,  
JR., CPA,**

**Respondent.**

**ORDER INSTITUTING PUBLIC  
ADMINISTRATIVE AND CEASE-  
AND-DESIST PROCEEDINGS PURSUANT TO  
SECTIONS 4C AND 21C OF THE SECURITIES  
EXCHANGE ACT OF 1934 AND RULE 102(e)  
OF THE COMMISSION'S RULES OF  
PRACTICE AND NOTICE OF HEARING**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate that public administrative and cease-and-desist proceedings be, and hereby are, instituted against Paul L. Chancey, Jr., CPA (“Respondent” or “Chancey”) pursuant to Sections 4C<sup>1</sup> and 21C of the Securities Exchange Act of 1934 (“Exchange Act”) and Rule 102(e)(1)(ii) of the Commission’s Rules of Practice.<sup>2</sup>

---

<sup>1</sup> Section 4C provides, in relevant part, that:

The Commission may censure any person, or deny, temporarily or permanently, to any person the privilege of appearing or practicing before the Commission in any way, if that person is found . . . (1) not to possess the requisite qualifications to represent others; (2) to be lacking in character or integrity, or to have engaged in unethical or improper professional conduct; or (3) to have willfully violated, or willfully aided and abetted the violation of, any provision of the securities laws or the rules and regulations issued thereunder.

<sup>2</sup> Rule 102(e)(1)(ii) provides, in pertinent part, that:

## II.

After an investigation, the Division of Enforcement and the Office of the Chief Accountant allege that:

### A. SUMMARY

1. Paul L. Chancey, Jr., a certified public accountant (“CPA”), engaged in improper professional conduct, within the meaning of Section 4C of the Exchange Act and Rule 102(e) of the Commission’s Rules of Practice, during the audits of the 2015 and 2016 financial statements of MiMedx Group, Inc. (“MiMedx”). MiMedx later restated these financial statements.

2. For both years, Chancey served as the lead audit engagement partner for Cherry Bekaert, LLP (“CB”), the accounting firm performing these audits, but he ignored evidence indicating that sales between MiMedx and one of its largest distributors (“Distributor”) were made on a consignment basis, and that MiMedx had therefore prematurely recognized revenue for these transactions at the time of shipment. For the 2015 audit, this evidence included written allegations from MiMedx’s controller that highlighted the consignment nature of these transactions and challenged MiMedx’s revenue recognition. For the 2016 audit, the Distributor itself explained the contingent payment terms for these transactions, demonstrating their consignment nature, in a confirmation response.

3. However, rather than considering the consignment nature of these transactions or performing additional audit procedures to determine if revenue on Distributor transactions was reported in conformity with generally accepted accounting principles (“GAAP”), and without documenting any analysis of the consignment issue in CB’s workpapers, Chancey improperly relied on MiMedx executives’ false representations that revenue recognition was appropriate. Chancey’s conduct violated several Public Company Accounting Oversight Board (“PCAOB”) standards, including standards requiring Chancey to act with due professional care and obtain sufficient, appropriate audit evidence.

4. Chancey also caused CB to violate Rule 2-02(b) of Regulation S-X. In connection with the 2015 and 2016 audits, CB issued audit reports in which it represented that CB had conducted the audits in accordance with the standards of the PCAOB, and further represented that, based on its opinion, MiMedx’s financial statements presented fairly, in all material respects, the company’s financial condition and results of its operations in conformity with GAAP. Chancey approved the issuance of CB’s audit reports that contained these unqualified opinions when he knew

---

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.

or should have known that CB's representations were false because CB's audits were not performed in accordance with PCAOB standards.

## **B. RESPONDENT**

5. **Paul L. Chancey, Jr.**, age 57, resides in Fayetteville, Georgia, and is a CPA licensed in Georgia and Mississippi. Chancey has been a partner at Cherry Bekaert, LLP, since 2006 and has less than a 5% ownership interest in the firm. Chancey was the lead engagement partner on each audit and interim review of MiMedx's financial statements from at least the first quarter of 2013 through the second quarter of 2017.

## **C. OTHER RELEVANT ENTITIES**

6. **Cherry Bekaert, LLP** is a limited liability company based in Richmond, Virginia, and a public accounting firm registered with the PCAOB. CB has 13 offices in the United States and more than 1,250 professional employees providing accounting, advisory, and consulting services. CB acted as MiMedx's independent auditor from June 9, 2008, to August 4, 2017. CB issued audit reports on the financial statements of MiMedx for each fiscal year from 2008-2016.

7. **MiMedx Group, Inc.** is a Florida corporation with its primary operations in Marietta, Georgia. MiMedx's stock is currently registered with the Commission under Section 12(g) of the Exchange Act and trades on the NASDAQ exchange under the symbol MDXG. The Commission previously charged MiMedx for, among other things, fraudulently misstating its 2015 and 2016 financial statements in violation of GAAP. The Commission accepted MiMedx's offer of settlement, whereby MiMedx consented to an order permanently enjoining future violations of certain securities laws and imposing a civil penalty of \$1.5 million. The district court entered final judgment against MiMedx on December 4, 2019. *See SEC v. MiMedx Group, Inc., et. al.*, No. 1:19-cv-10927-NRB (S.D.N.Y.).

## **D. FACTS**

### **Background**

8. MiMedx is a public company that sells medical products made from human placental tissue. MiMedx's 2015 and 2016 audited financial statements were included in filings MiMedx made with the Commission on Form 10-K. MiMedx's sales to customers in 2015 and 2016 included direct sales to distributors. MiMedx generally recognized revenue on those sales at the time of shipment.

9. CB was engaged by MiMedx as its independent auditor to conduct the annual audits of the 2015 and 2016 financial statements. CB's 2015 and 2016 audit reports contained unqualified opinions in which CB represented that it had conducted the audits in accordance with PCAOB audit standards, that MiMedx's financial statements fairly presented the financial condition and results of operations in all material respects, and that the financial statements had been prepared in conformity with GAAP.

10. As the lead audit engagement partner, Chancey had responsibility for the conduct of the audits, including planning, supervising team members, and ensuring compliance with PCAOB standards.

### **MiMedx Improperly Recognized Revenue on Transactions with Distributor**

11. Distributor arranged sales of MiMedx product to the U.S. Department of Veterans Affairs and U.S. Department of Defense medical facilities (collectively, the “VA”). MiMedx and Distributor had a written distribution agreement that provided that risk of loss passed to Distributor upon shipment of product, that Distributor had a specific number of days to pay invoices, and that Distributor could return product only if it was defective.

12. When Distributor and MiMedx first entered into this distribution agreement, Distributor purchased very limited quantities of MiMedx product and followed the terms of the written distribution agreement. MiMedx issued an invoice to Distributor upon shipment of product and recognized revenue at that time.

13. However, in late 2012, MiMedx asked Distributor to make bulk orders of product to stock at the VA. Distributor was willing to make bulk orders based on an arrangement that ensured Distributor would not be liable for payment to MiMedx until the VA used the products and committed to pay Distributor. As a result, MiMedx excused Distributor from payment until the VA issued a purchase order (“PO”) to Distributor for the product, which occurred after the VA used the product. This side arrangement was contrary to and replaced the terms of the written distribution agreement.

14. MiMedx also did not transfer risk of loss to Distributor until Distributor received a PO from the VA. Instead, MiMedx managed the inventory held at VA facilities and credited Distributor for any lost, dropped, or missing products stocked at the VA.

15. The side agreement between MiMedx and Distributor effectively transformed MiMedx’s arrangement with Distributor into one where the product was shipped on a consignment basis. As a result, under GAAP, MiMedx should have delayed recognizing revenue until it was realized or realizable and earned, which occurs only when each of the following conditions is met: (i) persuasive evidence of an arrangement exists; (ii) delivery has occurred or services have been rendered; (iii) the seller’s price to the buyer is fixed or determinable; and (iv) collectibility is reasonably assured. However, MiMedx improperly continued recognizing revenue upon shipment of the product, rather than delaying revenue recognition until Distributor was obligated to purchase the product.

16. The side arrangement, which lasted from at least late 2012 through 2017, was well known at MiMedx. MiMedx had a “Reconciliation Group” that closely tracked Distributor’s receipt of POs from the VA, which obligated the VA to pay Distributor for products used. Under the side arrangement, Distributor’s obligation to pay arose later than the MiMedx invoice date, which was contrary to the terms of the written distribution agreement.

17. Every weekday from late 2012 to the end of the relationship between MiMedx and Distributor in 2017, Distributor sent the Reconciliation Group a daily report listing each tissue for which the VA submitted a PO to Distributor. The Reconciliation Group then sent a daily email to MiMedx management providing the dollar value of the POs the VA had submitted to the Distributor. The Reconciliation Group then compiled the daily figures into a “Weekly Revenue” table circulated each Monday to MiMedx management and the accounting department.

18. Approximately 10 days after the close of each week, Distributor paid MiMedx the exact total cash amount identified in the Weekly Revenue table. The Reconciliation Group confirmed that Distributor’s payment matched the anticipated amount. Distributor paid MiMedx only the value of Distributor’s sales to the VA, its end customer.

19. MiMedx and Distributor agreed that Distributor’s payments would be applied to the oldest outstanding invoice, regardless of which specific products Distributor had sold through.

20. As a result of the side arrangement, MiMedx prematurely recognized revenue on transactions with Distributor for several years, including 2015 and 2016. Distributor was one of MiMedx’s largest customers, and sales to Distributor represented roughly 24% and 9% of MiMedx’s total revenue in 2015 and 2016, respectively.

21. In 2020, MiMedx restated its financial statements for several reporting periods due to its nonconformance with GAAP. MiMedx’s restatements included material changes for revenue prematurely recognized on sales to Distributor in 2015 and 2016.

### **Chancey Violated PCAOB Audit Standards When Conducting the 2015 and 2016 Audits**

22. During the audits of MiMedx’s 2015 and 2016 financial statements, CB and Chancey identified revenue as one of MiMedx’s most significant financial statement accounts and an area with heightened risk of material misstatement due to both error and fraud. PCAOB standards required CB to presume that improper revenue recognition was a fraud risk. Since revenue recognition was an area that required heightened scrutiny, CB had enhanced obligations under PCAOB standards to perform additional audit procedures.

23. MiMedx management made false representations to CB during each audit, in management representation letters and other documents, denying that MiMedx had a side arrangement with Distributor. During both the 2015 and 2016 audits, Chancey improperly relied on these management representations without appropriate corroboration, even though these representations directly contradicted information Chancey had received from reliable sources, including MiMedx’s controller and Distributor itself.

24. Chancey did not perform additional substantive audit procedures or obtain sufficient, appropriate audit evidence to reduce the risk of material misstatement to an

appropriately low level as required by PCAOB standards. Chancey's conduct demonstrated the following audit failures in violation of PCAOB standards: (1) failure to exercise due professional care; (2) failure to obtain an understanding of MiMedx's business; (3) failure to plan the audits based on assessment of risk; (4) failure to obtain sufficient appropriate audit evidence; (5) failure to evaluate audit results; and (6) failure to document audit work.

25. As a result of these violations, Chancey engaged in (1) a single instance of highly unreasonable conduct in circumstances for which heightened scrutiny is warranted; and (2) repeated instances of unreasonable conduct that indicate his lack of competence.

### **2015 Audit Failures**

26. Early in the 2015 audit, MiMedx's chief financial officer showed Chancey and MiMedx's Audit Committee an email from MiMedx's controller alleging improper revenue recognition relating to transactions with Distributor and others.

27. The controller alleged that Distributor "implicitly doesn't pay MiMedx until the tissue has been implanted, so revenue should be recognized on a consignment model." The controller referenced in his email "information[.]" "sales and collections data[.]" and "accounting research" that he had collected to support his conclusions.

28. Chancey read the email and knew about the controller's specific allegations, but Chancey made the decision not to obtain a copy of the controller's email for inclusion in the CB workpapers. Chancey also did not document, or ensure documentation of, the controller's allegations, or any related evaluation or resolution of the allegations, in the CB workpapers.

29. Chancey also knew that the controller declined to sign the management representation letter that CB had requested as part of its 2015 audit procedures. However, Chancey also did not document, or ensure documentation of, this significant fact in the CB workpapers.

30. Chancey never attempted to contact the controller to gain a better understanding of the controller's allegations, nor did Chancey request the supporting information the controller referenced in his email, even though CB was in regular contact with the controller in the course of performing 2015 audit procedures.

31. Chancey also did not attempt to obtain information about the possible consignment arrangement from Distributor, the VA, or even MiMedx personnel involved in collecting payments from Distributor.

32. While CB performed some testing during its audits, this testing was insufficient to allow CB to conclude whether MiMedx was appropriately recognizing revenue for its sales to Distributor. In particular, CB's procedures to test sales transactions, accounts receivable, the Days Sales Outstanding ("DSO") metric, the sales returns allowance, and sales commissions either failed to provide sufficient appropriate evidence that was relevant to the consignment issue or, instead, raised additional red flags or contradictory evidence suggesting that the arrangement with Distributor could be a consignment.

33. The DSO analysis, for example, reflected that Distributor was paying much later than, and in a manner that was not consistent with, the terms of the written distribution agreement. Additionally, the sales return allowance procedures reflected that the risk of loss had not transferred to Distributor upon shipment because MiMedx incurred losses for tissue that was subsequently lost, dropped, or missing. Further, the sales commissions procedures showed that MiMedx paid commissions to sales personnel only after the VA had implanted tissue, suggesting that the transaction was incomplete until that time.

34. MiMedx's Audit Committee conducted a limited review of the controller's allegations and concluded that MiMedx's accounting was appropriate based largely on the written distribution agreement, which MiMedx's management misrepresented as controlling the terms of the transactions with Distributor. Chancey attended an Audit Committee meeting where the Audit Committee reported the conclusions of its review, but he did not know what investigative steps the Audit Committee took in its review. Chancey did not implement any additional audit procedures to verify or corroborate the Audit Committee's work. Chancey also did not document, or ensure documentation of, the Audit Committee's review of the controller's allegations.

35. Despite the evidence he had, Chancey did not plan, perform, or document any additional substantive procedures for the 2015 audit to test whether a side arrangement with Distributor existed.

36. CB's 2015 workpapers did include a memo CB created as part of its audit procedures to summarize sales to Distributor. However, rather than documenting evidence obtained from substantive procedures performed to test the existence of a consignment arrangement, the memo referenced amendments to the written agreement that were not relevant and sales commission expense procedures that indicated a consignment arrangement might exist. The memo concluded, without sufficient basis, that "[c]onsistent with prior years, CB considers all four revenue recognition criteria to have been met on [Distributor's] sales."

37. At the conclusion of the 2015 audit, Chancey caused CB to issue an audit report that inaccurately stated that the audit was performed in accordance with PCAOB standards. MiMedx filed CB's inaccurate audit report with MiMedx's 2015 Form 10-K on February 29, 2016.

### **2016 Audit Failures**

38. During the 2016 audit, Chancey obtained new evidence, this time directly from Distributor, that further demonstrated MiMedx's consignment arrangement with Distributor.

39. In its 2016 accounts receivable audit confirmation response to CB, Distributor specifically stated that Distributor "does not pay MiMedx for tissues until such a time as the [VA] issues a purchase order to [Distributor]."

40. Also during the 2016 audit, Chancey learned that Distributor made the same representation (of payment due to MiMedx only upon the issuance of a PO from the VA) during a

MiMedx Audit Committee internal investigation into allegations of fictitious sales. As a result of that investigation, Chancey also learned that Distributor further represented that: (1) MiMedx had historically given Distributor credit for lost, dropped, and missing inventory; and (2) MiMedx applied Distributor's payments to the oldest invoices first, regardless of whether the VA made payments to Distributor for the products reflected in those invoices.

41. In addition, consistent with the evidence obtained in the 2015 audit, CB's procedures to test sales transactions, accounts receivable, the DSO metric, the sales returns allowance, and sales commissions either failed to provide sufficient appropriate evidence that was relevant to the consignment issue or, instead, raised additional red flags or contradictory evidence suggesting that the arrangement with Distributor was a consignment.

42. Despite this evidence, and the evidence from the 2015 audit, Chancey did not plan, perform, or document any additional substantive procedures for the 2016 audit to test whether a side arrangement existed. For example, he did not ask Distributor about the existence of a side arrangement or for any evidence Distributor might have to support its position that its obligation to pay MiMedx was contingent on a PO from the VA. Chancey also did not speak with anyone else at MiMedx or the VA who was involved in the sales and collection processes.

43. As part of its 2016 audit procedures, CB requested and obtained a revenue recognition memo from MiMedx management that supported MiMedx's revenue recognition for transactions with Distributor at the time of shipment. However, that memo did not provide sufficient appropriate evidence about revenue recognition considering the side agreement. Chancey improperly relied on management's representations that the written distribution agreement established the terms of the transactions, rather than performing incremental audit procedures specifically directed at testing the alleged side agreement.

44. At the conclusion of the 2016 audit, Chancey again caused CB to issue an audit report that inaccurately stated that the audit was performed in accordance with PCAOB standards. MiMedx filed CB's inaccurate audit report with MiMedx's 2016 Form 10-K on March 1, 2017.

### **PCAOB Audit Standards<sup>3</sup> Chancey Violated During the 2015 and 2016 Audits**

#### **Failure to Exercise Due Professional Care**

45. PCAOB AS 1015 (AU 230) Due Professional Care in the Performance of Work states, "the exercise of due professional care allows the auditor to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error

---

<sup>3</sup> Effective after the 2015 audit of MiMedx's financial statements, the PCAOB reorganized the structure and numbering of auditing standards. The reorganized standards did not impose new requirements or change the substance of the requirements on auditors. This document references the reorganized PCAOB auditing standards in effect during the audit of MiMedx's 2016 financial statements with the pre-reorganization references (related to the 2015 audit) provided parenthetically.



or fraud” and “[a]lthough not absolute assurance, reasonable assurance is a high level of assurance.” The standard requires the auditor to:

- a. exercise professional skepticism, “an attitude that includes a questioning mind and a critical assessment of audit evidence”;
- b. “consider the competency and sufficiency of the [audit] evidence”;
- c. neither assume that management is dishonest nor assume “unquestioned honesty” and “the auditor should not be satisfied with less than persuasive evidence because of a belief that management is honest”; and
- d. adhere to the standard during the planning and throughout the audit process.

46. PCAOB AS 2401 (AU 316) Consideration of Fraud in a Financial Statement Audit requires that the auditor exercise professional skepticism when considering fraud risks and “conduct the engagement with a mindset that recognizes the possibility that a material misstatement due to fraud could be present, regardless of any past experience with the entity and regardless of the auditor’s belief about management’s honesty and integrity. Furthermore, professional skepticism requires an ongoing questioning of whether the information and evidence obtained suggests that a material misstatement due to fraud has occurred.”

47. During both the 2015 and 2016 audits, Chancey had evidence that contradicted management representations about MiMedx’s transactions with Distributor. Yet, he improperly relied on management representations when concluding that MiMedx’s financial statements were free of material misstatement. Furthermore, Chancey failed to corroborate management representations or perform any additional substantive procedures to reconcile the contradictory evidence he had received from reliable sources and CB’s other audit procedures, and thus failed to reduce the risk of material misstatement to an appropriately low level.

48. As a result, Chancey failed to exercise due professional care, which was required by PCAOB standards, during the audits of MiMedx’s 2015 and 2016 financial statements.

#### **Failure to Obtain an Understanding of MiMedx’s Business**

49. PCAOB AS 1015 (AU 230) Due Professional Care in the Performance of Work requires that the engagement partner “be knowledgeable about the client.”

50. PCAOB AS 2110 (AS 12) Identifying and Assessing Risks of Material Misstatement requires the auditor to “obtain an understanding of the company and its environment (‘understanding of the company’) to understand the events, conditions, and company activities that might reasonably be expected to have a significant effect on the risks of misstatement.”

51. Chancey failed to become knowledgeable about MiMedx’s relationship with Distributor, which was one of MiMedx’s most significant customers. Among other things, Chancey failed to obtain an understanding of the following significant events, conditions, and activities impacting MiMedx’s transactions with Distributor:

- a. During the 2015 audit, the controller’s allegations about MiMedx’s consignment arrangement;

- b. During both the 2015 and the 2016 audits, Distributor’s practice of paying much later than the contract terms allowed;
- c. During both the 2015 and the 2016 audits, MiMedx’s practice of incurring losses for sales of tissue to Distributor, contrary to terms of the distribution agreement, when tissues were lost, dropped, or missing after shipment; and
- d. During the 2016 audit, Distributor’s representations that payment terms with MiMedx were contingent on sales to the VA.

52. As a result, Chancey failed to obtain an understanding of MiMedx’s business, which was required by PCAOB standards, during the audits of MiMedx’s 2015 and 2016 financial statements.

### **Failure to Plan the Audits Based on Assessment of Risk**

53. PCAOB AS 2101 (AS 9) *Audit Planning* states that “[p]lanning the audit includes establishing the overall audit strategy for the engagement and developing an audit plan, which includes, in particular, planned risk assessment procedures and planned responses to the risks of material misstatement. Planning is not a discrete phase of an audit but, rather, a continual and iterative process that might begin shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit.” Moreover, “[t]he auditor should modify the overall strategy and the audit plan as necessary if circumstances change significantly during the course of the audit, including changes due to a revised assessment of the risks of material misstatement or the discovery of a previously unidentified risk of material misstatement.”

54. PCAOB AS 2110 (AS 12) *Identifying and Assessing Risks of Material Misstatement* requires the auditor to “presume that there is fraud risk involving improper revenue recognition and evaluate which types of revenue, revenue transactions, or assertions may give rise to such risks.”

55. PCAOB AS 1101 (AS 8) *Audit Risk* provides that “reasonable assurance is obtained by reducing audit risk to an appropriately low level through applying due professional care, including obtaining sufficient appropriate audit evidence.”

56. During both the 2015 and 2016 audits, Chancey learned of red flags and contradictory evidence indicating that a side arrangement with Distributor existed, but CB did not perform additional procedures to determine if revenue was misstated. Even after Chancey learned during the 2015 audit that the controller had challenged MiMedx’s revenue recognition for transactions with Distributor and that the controller would not sign the management representation letter, and, during the 2016 audit, that Distributor had described its contingent payment terms with MiMedx in its audit confirmation response, Chancey did not modify CB’s audit plan to respond to the increased risk of material misstatement. This was true even though CB had previously identified revenue as an area with heightened risk of material misstatement due to error or fraud.

57. As a result, Chancey failed to plan the audits and revise risk assessments appropriately, as required by PCAOB standards, during the audits of MiMedx’s 2015 and 2016 financial statements.

### **Failure to Obtain Sufficient Appropriate Audit Evidence**

58. PCAOB AS 1105 (AS 15) Audit Evidence states that, “[t]o be appropriate, audit evidence must be both relevant and reliable in providing support for the conclusions on which the auditor’s opinion is based.” Relevance depends on “whether [the audit procedure] is designed to (1) test the assertion or control directly and (2) test for understatement or overstatement and the timing of the audit procedure used to test the assertion or control.” Additionally, “the reliability of evidence depends on the nature and source of the evidence and the circumstances under which it is obtained...Evidence obtained from a knowledgeable source that is independent of the company is more reliable than evidence obtained only from internal company sources.” Furthermore, the standard requires the auditor to:

- a. “plan and perform audit procedures to obtain sufficient appropriate audit evidence to provide a reasonable basis for his or her opinion”;
- b. “test the accuracy and completeness of the information” produced by the company; and
- c. “perform audit procedures necessary to resolve the matter” when “audit evidence obtained from one source is inconsistent with that obtained from another, or if the auditor has doubts about the reliability of information to be used as audit evidence” (emphasis added).

59. PCAOB AS 2805 (AU 333) Management Representations states that management representations “are not a substitute for the application of auditing procedures necessary to afford a reasonable basis for an opinion regarding the financial statements under audit” and, “[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” (emphasis added).

60. PCAOB AS 2310 (AU 330) The Confirmation Process explains that the purpose of confirmation is to obtain evidence from “third parties about financial statement assertions made by management.” The auditor should evaluate the evidence provided in the confirmation to obtain an understanding about the existence and details of significant oral modifications to written agreements and perform alternative procedures and additional testwork to obtain sufficient evidence. Further, nonresponses “do not provide audit evidence about the financial statement assertions being addressed.”

61. PCAOB AS 2301 (AS 13) The Auditor’s Responses to the Risks of Material Misstatement states that “assessed risks of material misstatement, particularly fraud risks, should involve the application of professional skepticism in gathering and evaluating audit evidence[,]” which includes “obtaining sufficient appropriate evidence to corroborate management’s explanations or representations concerning important matters.” The standard also requires the auditor to:

- a. design the audit procedures performed to “[o]btain more persuasive evidence the higher the auditor’s assessment of risk [and] [t]ake into account the types of potential misstatements that could result from the identified risks and the likelihood and magnitude of potential misstatement”;
- b. “perform substantive procedures for each relevant assertion of each significant account”;
- c. obtain more evidence from substantive procedures “as the assessed risk of material misstatement increases”; and
- d. modify the planned audit procedures, in response to fraud risk, “to obtain more reliable evidence regarding relevant assertions.”

62. PCAOB AS 2401 (AU 316) Consideration of Fraud in a Financial Statement Audit indicates that, if there is a risk of improper revenue recognition, the auditor consider “[c]onfirming with customers certain relevant contract terms and the absence of side agreements, because the appropriate accounting often is influenced by such terms or agreements. For example, acceptance criteria, delivery and payment terms, the absence of future or continuing vendor obligations, the right to return product, guaranteed resale amounts, and cancellation or refund provisions often are relevant in such circumstances.”

63. Chancey obtained reliable evidence from MiMedx’s controller during the 2015 audit, and from Distributor’s confirmation response during the 2016 audit, indicating that MiMedx and Distributor had a side arrangement. Additionally, during both audits, CB’s procedures concerning the DSO metric, the sales returns allowance, and sales commissions provided evidence suggesting that the arrangement MiMedx had with Distributor could be a consignment. This evidence contradicted MiMedx management’s representations claiming that the written distribution agreement controlled the terms of the transactions with Distributor.

64. Chancey failed to perform any incremental procedures to investigate the circumstances of this contradictory evidence or appropriately test the reliability of the representations made by MiMedx management. Chancey further failed to evaluate the contradictory audit evidence to obtain sufficient appropriate evidence for CB’s audit conclusions.

65. As a result, Chancey failed to obtain sufficient appropriate audit evidence, as required by PCAOB standards, during the audits of MiMedx’s 2015 and 2016 financial statements.

### **Failure to Evaluate Audit Results**

66. PCAOB AS 2810 (AS 14) Evaluating Audit Results requires the auditor to “obtain corroboration for management’s explanations regarding significant, unusual, or unexpected transactions, events, amounts, or relationships. If management’s responses to the auditor’s inquiries appear to be implausible, inconsistent with other audit evidence, imprecise, or not a sufficient level of detail to be useful, the auditor should perform procedures to address the matter” (emphasis added).

67. Because Distributor was one of MiMedx's largest distributors at the time, MiMedx's transactions with Distributor were significant. Despite the significance of the transactions, Chancey relied on management representations that were inconsistent with other audit evidence, without obtaining appropriate corroboration from other sources, during the audits of MiMedx's 2015 and 2016 financial statements. Although Chancey obtained contradictory evidence in two consecutive audits, he still failed to take action to reduce audit risk to an appropriately low level.

68. As a result, Chancey failed to evaluate audit results properly, as required by PCAOB standards, during the audits of MiMedx's 2015 and 2016 financial statements.

### **Failure to Document Audit Work**

69. PCAOB AS 1215 (AS 3) Audit Documentation requires the auditor to document:
- a. "significant findings or issues, actions taken to address them (including additional evidence obtained), and the basis for the conclusions reached in connection with each engagement";
  - b. "information the auditor has identified relating to significant findings or issues that is inconsistent with or contradicts the auditor's final conclusions" (emphasis added); and
  - c. "risks of material misstatement that are determined to be significant risks and the results of the auditing procedures performed in response to those risks."

70. During both the 2015 and 2016 audits, CB had reliable information that was inconsistent with CB's audit conclusions and raised significant risks about material misstatements in MiMedx's financial statements. However, Chancey failed to document, or ensure the documentation of, any analysis of the consignment issues raised and the basis for CB's audit conclusions in light of those issues. Notably, Chancey failed completely to document the controller's allegations and refusal to sign the management representation letter, much less any audit response to these issues, in CB's 2015 audit workpapers. He also failed to document in the 2016 audit workpapers any analysis or response to Distributor's representations about contingent sales terms. Furthermore, for both audits, he failed to document any analysis of the consignment issues raised by additional red flags and contradictory evidence obtained from the DSO analysis, the sales return allowance testwork, and the sales commission testwork.

71. As a result, Chancey failed to document audit work, as required by PCAOB standards, during the audits of MiMedx's 2015 and 2016 financial statements.

### **CB's Inaccurate Audit Reports**

72. Despite Chancey's multiple departures from PCAOB audit standards, as described above, CB, through Chancey, issued audit reports that contained unqualified opinions on MiMedx's 2015 and 2016 financial statements. Those reports contained CB's opinion that MiMedx's financial statements presented fairly, in all material respects, the company's financial

position and results of operations in conformity with GAAP, and CB's representation that its audits were conducted in accordance with PCAOB audit standards.

73. As the lead engagement partner on the audits, Chancey approved the issuance of these audit reports. Chancey knew that MiMedx would file CB's audit reports with the Commission with MiMedx's Forms 10-K.

74. Chancey caused CB's audit reports to inaccurately state that the audits were conducted in accordance with PCAOB audit standards.

## **E. VIOLATIONS**

75. As a result of the conduct described above, Chancey engaged in improper professional conduct within the meaning of Exchange Act Section 4C(a)(2) and Rule 102(e)(1)(ii) of the Commission's Rules of Practice. Section 4C(a)(2) and Rule 102(e)(1)(ii) provide, in pertinent part, that the Commission may censure or deny, temporarily or permanently, the privilege of appearing or practicing before the Commission to any person who is found by the Commission to have engaged in improper professional conduct. Exchange Act Section 4C(b) and Rule 102(e)(1)(iv) define improper professional conduct with respect to persons associated with public accounting firms and persons licensed to practice as accountants, respectively, as (1) a single instance of highly unreasonable conduct in circumstances for which heightened scrutiny is warranted; or (2) repeated instances of unreasonable conduct that indicate a lack of competence.

76. As a result of the conduct described above, Chancey caused the violation of Rule 2-02(b)(1) of Regulation S-X, which requires an audit report to accurately state whether the audit was made in accordance with generally accepted auditing standards. The phrase "generally accepted auditing standards" refers to the standards issued by the PCAOB. *See* Act Rel. No. 33-8422. Under Exchange Act Section 21C, a person is a "cause" of another's primary violation if the person knew or should have known that his act or omission would contribute to the primary violation.

## **III.**

In view of the allegations made by the Division of Enforcement and the Office of the Chief Accountant, the Commission deems it necessary and appropriate in the public interest that public administrative and cease-and-desist proceedings be instituted to determine:

A. Whether the allegations set forth in Section II hereof are true and, in connection therewith, to afford Respondent an opportunity to establish any defenses to such allegations;

B. What, if any, remedial action is appropriate against Respondent pursuant to Section 4C of the Exchange Act and Rule 102(e)(1) of the Commission's Rules of Practice; and

C. Whether, pursuant to Section 21C of the Exchange Act, Respondent should be ordered to cease and desist from committing or causing violations of and any future violations of

Rule 2-02(b)(1) of Regulation S-X, and whether Respondent should be ordered to pay a civil penalty pursuant to Section 21B(a) of the Exchange Act.

#### IV.

IT IS ORDERED that a public hearing before the Commission for the purposes of taking evidence on the questions set forth in Section III hereof shall be convened not earlier than 30 days and not later than 60 days from service of this Order at a time and place to be fixed by further order of the Commission, pursuant to Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that Respondent shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice, 17 C.F.R. § 201.220(b).

IT IS FURTHER ORDERED that the Division of Enforcement and Respondent shall conduct a prehearing conference pursuant to Rule 221 of the Commission's Rules of Practice, 17 C.F.R. § 201.221, within fourteen (14) days of service of the Answer. The parties may meet in person or participate by telephone or other remote means; following the conference, they shall file a statement with the Office of the Secretary advising the Commission of any agreements reached at said conference. If a prehearing conference was not held, a statement shall be filed with the Office of the Secretary advising the Commission of that fact and of the efforts made to meet and confer.

If Respondent fails to file the directed Answer, or fails to appear at a hearing or conference after being duly notified, the Respondent may be deemed in default and the proceedings may be determined against him upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f), and 201.310.

This Order shall be served forthwith upon Respondent by any means permitted by the Commission's Rules of Practice.

The Commission finds that it would serve the interests of justice and not result in prejudice to any party to provide, pursuant to Rule 100(c) of the Commission's Rules of Practice, 17 C.F.R. § 201.100(c), that notwithstanding any contrary reference in the Rules of Practice to service of paper copies, service to the Division of Enforcement of all opinions, orders, and decisions described in Rule 141, 17 C.F.R. § 201.141, and all papers described in Rule 150(a), 17 C.F.R. § 201.150(a), in these proceedings shall be by email to the attorneys who enter an appearance on behalf of the Division, and not by paper service.

Attention is called to Rule 151(a), (b) and (c) of the Commission's Rules of Practice, 17 C.F.R. § 201.151(a), (b) and (c), providing that when, as here, a proceeding is set before the Commission, all papers (including those listed in the following paragraph) shall be filed electronically in administrative proceedings using the Commission's Electronic Filings in Administrative Proceedings (eFAP) system access through the Commission's website,

[www.sec.gov](http://www.sec.gov), at <http://www.sec.gov/eFAP>. Respondent also must serve and accept service of documents electronically. All motions, objections, or applications will be decided by the Commission.

The Commission finds that it would serve the interests of justice and not result in prejudice to any party to provide, pursuant to Rule 100(c) of the Commission's Rules of Practice, 17 C.F.R. § 201.100(c), that notwithstanding any contrary reference in the Rules of Practice to filing with or disposition by a hearing officer, all filings, including those under Rules 210, 221, 222, 230, 231, 232, 233, and 250 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.210, 221, 222, 230, 231, 232, 233, and 250, shall be directed to and, as appropriate, decided by the Commission. This proceeding shall be deemed to be one under the 120-day timeframe specified in Rule of Practice 360(a)(2)(i), 17 C.F.R. § 201.360(a)(2)(i), for the purposes of applying Rules of Practice 233 and 250, 17 C.F.R. §§ 201.233 and 250.

The Commission finds that it would serve the interests of justice and not result in prejudice to any party to provide, pursuant to Rule 100(c) of the Commission's Rules of Practice, 17 C.F.R. § 201.100(c), that the Commission shall issue a decision on the basis of the record in this proceeding, which shall consist of the items listed at Rule 350(a) of the Commission's Rules of Practice, 17 C.F.R. § 201.350(a), and any other document or item filed with the Office of the Secretary and accepted into the record by the Commission. The provisions of Rule 351 of the Commission's Rules of Practice, 17 C.F.R. § 201.351, relating to preparation and certification of a record index by the Office of the Secretary or the hearing officer are not applicable to this proceeding.

The Commission will issue a final order resolving the proceeding after one of the following: (A) The completion of post-hearing briefing in a proceeding where the public hearing has been completed; (B) The completion of briefing on a motion for a ruling on the pleadings or a motion for summary disposition pursuant to Rule 250 of the Commission's Rules of Practice, 17 C.F.R. § 201.250, where the Commission has determined that no public hearing is necessary; or (C) The determination that a party is deemed to be in default under Rule 155 of the Commission's Rules of Practice, 17 C.F.R. § 201.155, and no public hearing is necessary.

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Vanessa A. Countryman  
Secretary