UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 57381 / February 26, 2008

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2792 / February 26, 2008

ADMINISTRATIVE PROCEEDING
File No. 3-12971

In the Matter of **NICHOLAS DIFAZIO, CPA,** **Respondent.**	**ORDER INSTITUTING PUBLIC ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that public administrative proceedings be, and hereby are, instituted against Nicholas Difazio, CPA ("Respondent" or "Difazio") pursuant to Rule 102(e)(1)(ii) of the Commission's Rules of Practice.[1]

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Public

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

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

Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[2] that:

A. SUMMARY

This Order concerns the conduct of Nicholas Difazio, an audit partner at Deloitte & Touche LLP ("D&T"), in connection with fiscal year 2000 and 2001 audits of the financial statements of Delphi Corporation ("Delphi"). On October 30, 2006, the Commission brought actions against Delphi and 13 individuals in connection with their role in widespread accounting violations at Delphi. Difazio, then the lead engagement partner on the Delphi audits, engaged in improper professional conduct, as detailed below.

B. RESPONDENT

Nicholas Difazio, 44, a resident of Bloomfield, Michigan, has been an audit partner at D&T since 1995 and served as lead client service partner on the Delphi engagement for the fiscal year 1999 through 2002 audits of Delphi's financial statements. In that role, Difazio was directly responsible for providing audit services, and oversaw the provision of tax, mergers and acquisitions and consulting services, to Delphi. He currently serves in D&T's New York office. Difazio has been licensed as a CPA in the State of Michigan since 1987 and in the State of New York since 2003.

C. FACTS

1. Difazio's Review and Audit of Delphi Warranty Costs Charged to Equity

In the second quarter of 2000, Delphi misclassified a $112 million increase in its warranty reserves as a charge to stockholders' equity, rather than to current-period warranty expenses, as required by Generally Accepted Accounting Principles ("GAAP"). The misclassification was reflected in Delphi's second quarter 2000 Form 10-Q and in its fiscal year 2000 Form 10-K. Delphi's improper treatment of the warranty reserve allowed it to increase the reserve and avoid a material increase in expenses. Later, Delphi restated the accounting for this transaction and D&T signed off on the restatement.

Delphi was spun-off from its former parent effective January 1, 1999. By May 2000, Delphi's former parent company had asserted as much as $800 million in warranty claims under Delphi's supply agreement with the former parent company. Many claims related to parts that Delphi had manufactured and the former parent company had incorporated into its products prior to Delphi's spin-off from the former parent company in 1999. Delphi disputed the former parent company's right to recover these warranty costs, but ultimately determined during the second

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

quarter of 2000 that it would likely offer the former parent company $100 million to settle the claims. Delphi incorrectly accounted for the warranty claims using an accounting method afforded to certain post-employment benefit liabilities that received special treatment under the agreement governing the spin-off of Delphi from the former parent company. Payments from Delphi to the former parent company made within one year of the spin-off to offset the "true up" of those post-employment benefit liabilities were accounted for as a direct charge to Delphi's shareholders' equity, rather than as a charge to income, and certain other adjustments were similarly charged directly to equity because they were considered to be the resolution of open items in accordance with the original intent of the agreement between Delphi and its former parent. Delphi treated the warranty claims by the former parent company the same way: Delphi recorded an increase to its warranty reserve of approximately $112 million, and improperly accounted for the accrual as a charge to stockholders' equity of $69 million, which was $112 million net of taxes.

Difazio should not have accepted Delphi's view that it could use these special accounting rules and not the accounting rules that apply broadly to contingencies and changes in estimates on this warranty matter. Although Difazio provided a memorandum regarding the transaction to the Concurring Review Partner with regard to this warranty matter, he did not consult with D&T's national office concerning Delphi's application of the special spin-off accounting treatment to the former parent company's warranty claims. Delphi's warranty liability did not qualify for such special treatment. Although the warranty claims related to parts produced by Delphi prior to the spin-off, and were referred to as such by the parties, they arose in the normal course of the customer-supplier relationship between Delphi and the former parent company. The spin-off agreement expressly provided that Delphi was liable for warranty defects, regardless of a part's date of manufacture, and did not include provisions comparable to the true-up mechanism for post-employment benefits. Under these circumstances, changes in the estimated warranty liability should have been accounted for through the income statement of the current period, in accord with Statement of Financial Accounting Standards ("SFAS") No. 5, "Accounting for Contingencies." Difazio did not correctly identify the appropriate accounting guidance for the warranty accrual and unreasonably accepted Delphi's method which avoided recognition of the warranty expense. For these reasons, Difazio's audit did not conform to Generally Accepted Auditing Standards ("GAAS").

2. Difazio's Review and Audit of the September 2000 Settlement Agreement

In the third quarter of 2000, Delphi paid the former parent company $237 million to resolve its warranty claims. Delphi misclassified $202 million of the $237 million payment to the former parent company as relating to pension and other post-employment benefits rather than warranty expense. This enabled Delphi to avoid recognizing the warranty expense in the third quarter and instead to defer that charge over many years. By accounting for only $35 million of the payment as settlement of warranty issues and the remaining $202 million as a pension "actuarial loss" that would be amortized as a charge to earnings over the next decade or more, Delphi did not comply with GAAP.

By September 2000, Delphi determined to pay the former parent company to settle 27 identified warranty claims, and it drafted a settlement agreement according to which Delphi would

pay the former parent company $237 million, which, unknown to Difazio, was the parties' estimate of the present value of Delphi's share of the former parent company's anticipated warranty outlays. Although the agreement negotiated orally between the parties covered only warranty claims, Delphi's management drafted and the former parent company signed a written settlement agreement, dated September 22, 2000, that mischaracterized the $237 million settlement as resolving two issues – warranty claims and increased pension and other post-employment benefit costs due to changes in healthcare assumptions – instead of just warranty claims. Three weeks before the agreement was executed, Delphi management discussed with Difazio a request by its former parent for adjustments to offset certain healthcare and other cost trends. Prior to the consultation, a Delphi manager had mentioned to Difazio that the former parent was expected to raise such an issue. Difazio did not know, however, that the former parent company had never asserted a claim involving changes in healthcare assumptions. In fact, the former parent company believed the separation agreements governing Delphi's spin-off from the former parent company would not allow such a claim. Delphi management told Difazio that it intended to attribute $202 million of the $237 million to the release of true-up assumption claims.[3] As support for its valuation of the other post-employment benefit claims, Delphi furnished Difazio with the deceptive written agreement and a September 6, 2000, letter from an actuarial consultant stating that $202 million was a "rough estimate of the impact" of using certain updated and forecasted assumptions for healthcare claims and health care trend rates in the calculation of the true-up between Delphi and the former parent company.

When Delphi presented the executed agreement as simultaneously settling two issues, Difazio should have made greater inquiry into Delphi's representations supporting the allocation which was now necessary. Difazio should have known that the separation agreements provided that the 1998 assumptions should be used for the true-up calculations. Difazio did not request or receive any documentation of the former parent company's purported claim or any legal assessment of its merits, and instead relied on the representations of members of Delphi management whom he believed were knowledgeable about the negotiations. Difazio should have known that updating the assumptions would result in Delphi's paying that incremental cost for employees assigned to the former parent company, even though the spin-off agreement limited Delphi's responsibility to benefits earned by its own employees who were active at the spin-off date and had not retired during a brief period following the spin-off.

Difazio also placed undue reliance on Delphi's actuarial consultant in support of the reasonableness of the other post-employment benefit claim. Although he had oral discussions with the actuary in which the actuary explained the calculation and his understanding of the agreement, Difazio should have known that the actuary did not participate in any negotiations with the former parent company and therefore could only be relaying information received from Delphi, and that the actuary was not interpreting Delphi's agreements with the former parent company, but merely performing a requested calculation using inputs provided by Delphi. Moreover, D&T requested a separate letter from the actuary during its year-end audit to confirm the valuation in the settlement agreement and the approach used in determining the amount. In response, the actuary faxed a copy

[3] True-up calculations were designed to restore Delphi to its initially agreed-upon capitalization as of January 1, 1999, after adjustments for the post-employment liabilities recorded for employees that returned to Delphi's former parent company or retired as former parent company employees during a window period.

of its original September 6 letter with a cover sheet noting: "Attached is a note we prepared in September regarding the impact of alternative actuarial assumptions on certain true-up amounts. Please see [Delphi] for further information regarding the September agreement." In accordance with Delphi's instruction, the actuary included the amount Delphi attributed to resolution of the post-employment assumptions within the deferred pension balances in his year-end valuation. Difazio unreasonably concluded that the actuary's sending a copy of the original September 6 letter and the year-end valuation was sufficient confirmation.

Additionally, in connection with the $237 million payment, Difazio unreasonably did not object to Delphi's method of allocating the settlement, and Difazio did not gather evidence as to whether the $202 million allocation reflected the fair value of the release in the settlement agreement. Further, Difazio unreasonably relied on Delphi's warranty cost experience as a wholly owned subsidiary as evidence supporting the residual attribution of $35 million to the 27 settled warranty claims, despite his awareness that the parent company's claims against Delphi as an independent company could be different.

In addition, Difazio failed to apply adequate professional skepticism in light of indications that the former parent company could be accounting for a much greater portion of the $237 million as payment for the former parent company's warranty claims against Delphi. First, Difazio did not sufficiently scrutinize a "clawback" provision in the settlement agreement under which, if the former parent company's warranty expense turned out to be less than anticipated, Delphi might be able to recover from the former parent company amounts in excess of the $35 million it supposedly paid for warranty. Difazio also failed to recognize the implications of a side letter to the agreement which was necessary only because the former parent company and Delphi both understood that the former parent company would be treating the $237 million as a warranty payment and that this would have certain tax implications relating to the spin-off.[4] Finally, Difazio did not perform any additional procedures in response to a call from the lead D&T engagement partner on the audit of the former parent company that he received after the opinion on Delphi's fiscal year 2000 financial statements had been issued. The engagement partner told Difazio to make sure he had documentation for the accounting position taken by Delphi. In light of this call, Difazio should have made further inquiries prior to the subsequent reissuance of D&T's audit report for fiscal year 2000 in Delphi's May 2001 prospectus offering debt securities.

In sum, Difazio's performance on the Delphi audit was deficient because he did not challenge sufficiently Delphi's unreasonable approach to the allocation of the settlement amount or gather sufficient evidence supporting the allocation. Difazio mistakenly assured the Delphi audit committee regarding the completeness of D&T's review of the settlement agreement and that D&T

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[4] For liquidity reasons, Delphi could not pay $237 million in addition to a previously agreed $800 million for true-up. The former parent company was willing to defer part of the amount due from Delphi, but the tax-free status of the spin-off would have been jeopardized if the amount deferred related to warranty reimbursement rather than the true-up agreement. Therefore, the former parent company and Delphi executed a separate agreement in conjunction with the settlement agreement specifying that $237 million of the $800 million true-up payment would be deferred, and that Delphi would immediately pay the $237 million due under the settlement agreement. Difazio should have recognized that this side agreement would not have been necessary had the former parent company also intended to account for the bulk of the settlement payment as relating to true-up.

believed it had obtained sufficient evidence to conclude that "the accounting is reasonable." In reality, for the reasons given above, Difazio's audit did not conform to GAAS.

3. Difazio's Response to New Information Concerning the Repurchase of Generator Cores and Batteries from the Consulting Company

In a December 27, 2000 transaction, Delphi purported to sell $70 million of bulk inventories consisting of substantially all of Delphi's inventories of generator cores and finished automotive batteries to a company that was primarily engaged in providing consulting assistance to troubled automotive industry suppliers and automotive companies engaged in turnaround efforts (the "Consulting Company"). The written agreement between Delphi and the Consulting Company expressly stated that it constituted the entire agreement, and that any oral discussions in connection with the agreement were not enforceable. The written agreement contained no commitment to repurchase the cores or batteries. Nevertheless, pursuant to an oral side agreement made at the time of the original sale and not revealed to D&T or Difazio, Delphi purchased the identical inventory of cores and batteries back from the Consulting Company on January 5, 2001, at its original price, plus a transaction fee. Because Delphi committed to repurchase the cores and batteries at a price that covered the Consulting Company's costs and paid it a fee, GAAP required the arrangement to be accounted for as a product financing under SFAS No. 49, but Delphi improperly accounted for the transactions as a separate sale and purchase. Delphi did not recognize any revenue or direct profit on the sale, but nevertheless recognized $27 million in last in, first out ("LIFO") inventory liquidation gains, which were included by Delphi as part of its year-end disclosure of $96 million in LIFO gains that Delphi attributed in part to "aggressive inventory management."

A D&T partner other than Difazio performed and documented the year-end audit procedures in connection with this transaction. However, Difazio was aware of the transaction and his notes prepared for January and February 2001 audit committee meetings describe his understanding that the sale of the generator cores was in anticipation of a sale of the generator business with which the inventory was associated.

Later, however, in the course of D&T's review of Delphi's first quarter 2001 financial statements, in April or May 2001, Difazio became aware that at least a significant portion of the generator cores sold in the final days of 2000 had been repurchased during the first quarter. As part of his quarterly review, Difazio asked senior members of Delphi's management why a repurchase had occurred, and was told that Delphi had changed its view as to its need for possession of the cores in light of its plans regarding the sale of the generator business. Delphi management also orally reaffirmed to Difazio that there had been no prior repurchase commitment to the Consulting Company. Difazio accepted this explanation, based on the facts known to him, but did not document his consideration of this issue, and performed no additional procedures.

The response of Difazio to the discovery of inventory repurchased in the first quarter so soon after the year-end bulk sale, particularly in the face of a prior management representation that there was no obligation to repurchase the inventory, was inadequate. It indicated insufficient concern about facts that could have contradicted important management representations or otherwise indicated the possible presence of fraud. Difazio recalls knowing that "some" inventory

was repurchased at some time in the first quarter, but had no recollection that the sale or repurchase also involved batteries. Difazio had a duty in those circumstances to learn more about the unexpected repurchase so that the inquiries of management could be sufficiently probative, but he did not seek out additional facts. D&T's work papers showed that the repurchase comprised all, or substantially all, of the original bulk sale of both generator cores and batteries. The invoice for the repurchase, which D&T neither requested nor received, showed that it occurred nine days after the sale. The invoice price, compared to the original sale price, showed that the purported value of the inventory increased over those nine days (representing the fee to the Consulting Company). In addition, Delphi's records reveal that Delphi itself had provided the cash with which the Consulting Company purchased the inventories. In light of facts which were known to him, GAAS required Difazio to make additional inquiries or conduct additional procedures.

D. VIOLATIONS

Rule 102(e)(1)(ii) provides that the Commission may temporarily or permanently deny an accountant the privilege of appearing or practicing before it, if it finds, after notice and opportunity for hearing, that the accountant engaged in "improper professional conduct." Such improper professional conduct includes, as applicable here, negligent conduct, defined as "repeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards, that indicate a lack of competence to practice before the Commission." Rule 102(e)(1)(iv)(A)-(B). Difazio failed (i) to obtain sufficient competent evidential matter to afford a reasonable basis for the opinion rendered, Auditing Standards §AU 326, (ii) to exercise due professional care in the planning and performance of the audit, Auditing Standards § AU 230, and (iii) in performing the audit to identify material departures from GAAP in the financial statements, Auditing Standards § AU 410. In addition, he wrongly stated that the audit conformed to GAAS, Auditing Standards § AU 508. As a result of the actions detailed above, for Delphi's fiscal year 2000 and 2001, Difazio engaged in improper professional conduct on the second and third quarter 2000 warranty and batteries/cores transactions.

E. FINDINGS

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

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent Difazio's Offer.

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

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

B. After three (3) years from the date of this order, Respondent may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

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

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

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

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

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

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

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

if state licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Respondent's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Nancy M. Morris
Secretary