

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9573 / April 8, 2014

SECURITIES EXCHANGE ACT OF 1934
Release No. 71896 / April 8, 2014

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3548 / April 8, 2014

ADMINISTRATIVE PROCEEDING
File No. 3-15825

In the Matter of

LAIRD DANIELS, CPA,

Respondent.

**ORDER INSTITUTING PUBLIC
ADMINISTRATIVE AND
CEASE-AND-DESIST PROCEEDINGS
PURSUANT TO SECTION 8A OF THE
SECURITIES ACT OF 1933,
SECTIONS 4C AND 21C OF THE
SECURITIES EXCHANGE ACT OF 1934,
AND RULE 102(e) OF THE
COMMISSION'S RULES OF PRACTICE,
MAKING FINDINGS, AND IMPOSING
REMEDIAL SANCTIONS AND A
CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted against Laird Daniels ("Respondent" or "Daniels") pursuant to Section 8A of the Securities Act of 1933 ("Securities Act"), Sections 4C and 21C of the Securities Exchange Act of 1934 ("Exchange Act"), and Rule 102(e)(1)(iii) of the Commission's Rules of Practice.

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

Administrative and Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933, Sections 4C and 21C of the Securities Exchange Act of 1934, and Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

III.

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

A. SUMMARY

In the third quarter of 2009, CVS Caremark Corporation ("CVS") dramatically and without public disclosure changed its accounting for 525 Longs drugstores that had been acquired in October 2008. CVS improperly reduced the value of \$189 million of personal property in the Longs stores down to \$0. CVS then reversed \$49 million of depreciation that had been taken on those assets since the acquisition. The undisclosed depreciation reversal increased third-quarter 2009 earnings per share ("EPS") by approximately 2.4¢, enabling CVS to exceed analysts' expectations at a time when it was announcing a significant reduction in its earnings projections for 2010. With proper accounting, the asset write-down would have been treated as a current-period expense, and third-quarter 2009 EPS would have been reduced by as much as 17% (as much as 9.3¢).

Respondent Daniels, then the Retail Controller at CVS, orchestrated the improper accounting adjustment, causing CVS to value at \$0 all the personal property in approximately 430 of the 525 Longs stores, including more than 360 stores that CVS was going to operate for the long term. In Daniels' own words, CVS's accounting turned the acquisition of the Longs drugstores from a "bad guy" into a "good guy."

B. RESPONDENT

Daniels is 44 years old and lives in North Attleboro, Massachusetts. He is licensed in Connecticut as a certified public accountant. Prior to May 2009, he was Vice President for Corporate Budgeting at CVS, with responsibility for preparing budgets and forecasts for its retail pharmacy business. In May 2009, he became Retail Controller, with responsibility for collecting financial information from units within the retail pharmacy business and supervising the preparation of budgets, actual financial results, and forecasts. In January 2010, he became Chief Accounting Officer, with responsibility for the consolidation of financial information for all segments of CVS. He is currently the Senior Vice President for International Operations and Business Development at CVS.

C. OTHER RELEVANT ENTITY

CVS is a Delaware corporation with its principal executive offices in Woonsocket, Rhode Island. Its common stock is traded on the New York Stock Exchange under the symbol "CVS." It operates a nationwide chain of more than 7,400 drugstores and currently ranks #13 on the Fortune 500 list, with more than \$120 billion of revenue in 2012.

D. DANIELS ORCHESTRATED IMPROPER ADJUSTMENTS TO THE ACCOUNTING FOR THE LONGS ACQUISITION

Introduction

1. On October 20, 2008, CVS acquired the Longs chain of approximately 525 drugstores. CVS hired a major accounting firm to prepare a valuation for the Longs purchase price accounting (“PPA”) under Statement of Financial Accounting Standards (“SFAS”) 141 (“Business Combinations”).¹ On January 27, 2009, the valuation firm submitted a draft report. As required by its contract with CVS, the valuation firm applied a “continued use” premise – that CVS would retain and continue using all of the Longs stores’ property, plant and equipment (except for stores to be closed, as identified by CVS). The firm valued the Longs stores’ property, plant and equipment at more than \$1.2 billion, including \$937 million of real property and \$229 million of personal property. The valuation results were included in CVS’s audited financial statements for the fiscal year ended December 31, 2008, which were incorporated by reference in the annual report on Form 10-K that CVS filed with the Commission on February 27, 2009.

2. After accounting for the Longs PPA in its financial statements for 2008 and the first and second fiscal quarters of 2009, CVS, through Daniels, improperly adjusted the way the Longs PPA was accounted for and included the improper adjustments to the Longs PPA in later financial statements filed in November 2009. The result of this change was to boost CVS’s financial results for its quarter ended September 30, 2009 (its third quarter).

3. On November 5, 2009, CVS filed with the Commission a quarterly report on Form 10-Q for its third quarter ended September 30, 2009 containing unaudited financial statements that included adjustments to the Longs PPA. Compared to the valuation firm’s January 2009 draft report, the value of Longs tangible assets was reduced by \$212 million and goodwill was increased by the same amount. The reduction of tangible assets resulted primarily from a \$189 million decrease in the value of the Longs stores’ personal property (from \$229 million to \$40 million). Despite the “continued use” premise that had been built into the valuation firm’s January 2009 draft report, CVS now completely wrote off all personal property in approximately 430 of the 525 Longs stores, including more than 360 stores that were going to be operated for the long term.

4. In its third-quarter 2009 unaudited financial statements, CVS made a one-time catch-up adjustment reversing \$49 million of the depreciation that had been taken on Longs personal property from October 20, 2008 through June 30, 2009, and it did not take an additional \$19 million of depreciation that would otherwise have been taken on Longs personal property in the third quarter. The one-time depreciation reversal increased CVS’s third-quarter 2009 earnings per share (“EPS”) by approximately 2.4¢.²

5. The Longs PPA adjustments did not comply with generally accepted accounting principles (“GAAP”), specifically SFAS 141, because: (1) they did not reflect the expected future use of the Longs personal property as of the acquisition date in October 2008; (2) they did not

¹ SFAS 141 was superseded by SFAS 141R as of December 2008 – two months after the Longs acquisition.

² CVS emphasizes, and analysts usually focus on, the company’s “adjusted” EPS – GAAP EPS minus amortization and net of tax. All references to EPS in this Order are to adjusted EPS.

reflect information that CVS knew or had arranged to obtain as of the acquisition date; and (3) they did not account for CVS's use of the assets to generate revenue after the acquisition date. The failure to comply with GAAP had a material impact on the company's third-quarter 2009 financial results.

6. Between the time that CVS initially included the Longs PPA in its 2008 financial statements and the time it adjusted the Longs PPA in its financial statements for the 2009 third quarter, Daniels took a series of steps to improperly alter the Longs PPA in order to get a more positive accounting impact for CVS.

7. On June 16, 2009, Daniels told a co-worker that he had been making "some good progress on the tangible asset side" with the valuation firm and that he was now "extremely confident (by the way that's the most confident I get) that the final valuation will no longer be a bad guy but rather a good guy." (Daniels routinely used the terms "good guy" and "bad guy" to indicate whether an item improved or harmed CVS's purported profitability.)

The Original Purchase Price Allocation for the Longs Acquisition

8. In November 2008, CVS hired a major accounting firm to prepare a valuation for the Longs PPA. The engagement letter specified that, applying SFAS 141, the firm would determine the "fair value" of the Longs assets "as part of a 'going concern in continued use,'" and that "this valuation premise presupposes the continued utilization of the assets in connection with all other assets as the highest and best use." The engagement letter called for the firm to submit "Phase One" summary schedules by December 31, 2008 and a draft "Phase Two" report three weeks later.

9. On November 4, the valuation firm asked CVS for certain information about the Longs tangible assets, including "Information regarding any future use / development / refurbishment projects at existing stores. List of rationalization / store closure plans."

10. On December 14, Daniels (who was then the Director of Budgeting and Forecasting) told the CVS real estate group to provide the valuation firm with the latest strategy for using the Longs drugstores, adding "I know it's not final but I assume it's pretty close."

11. On December 15, the Real Estate Finance Director provided the valuation firm with the current strategy for each Longs store, along with a cover email from a manager in the real estate group stating, "I don't expect many changes." The list indicated that CVS planned to close 36 stores right away, relocate 19 stores within one year, operate 123 stores with the intent to relocate them within three years (if possible), and operate 349 stores for the long-term. Soon after, the Finance Director told another manager in the real estate group that the December 15 list was "predominately finished, but will have limited ongoing changes."

12. The valuation firm's approach to determining the "fair value" of the tangible assets in the Longs stores depended on CVS's intended use of each store.

a. For assets in the stores to be operated for more than one year, the firm applied a "continued use" premise. The firm determined the "direct replacement cost" for the leasehold improvements and the furniture, fixtures and equipment ("FF&E") in each store, using

data from the CVS real estate group that a typical new CVS store had fixed costs of \$45,101 and variable costs of \$38.77 per square foot. The firm applied an “indirect cost approach” (historical cost trended forward) for the computer equipment and the assets in the Longs corporate locations.

b. For the assets in the stores to be closed within one year, the firm determined the “orderly liquidation value” using data from the CVS real estate group indicating that approximately 35% of the assets would have liquidation value.

13. On December 23, the valuation firm sent draft schedules to the Retail Controller (Daniels’ predecessor in this position). For the Longs drugstores, the real property was valued at \$937.2 million and the personal property was valued at \$229.3 million. These schedules were the “Phase One” summary schedules required by the engagement letter. The Retail Controller forwarded the schedules to CVS’s outside auditors.

14. On January 12, 2009, the Retail Controller asked the valuation firm for “updated valuation schedules that reflect all changes to date.” He also stated, “We are entering the danger zone on closing the year. If there are any significant open items affecting the current valuation estimates, we have to resolve them tomorrow.” Minutes later, a Senior Manager at the valuation firm replied that, on a recent call with CVS’s outside auditors, “all of the major issues were discussed and agreed to, which would mean leaving our analysis as is.”

15. On January 13, the valuation firm sent updated schedules to the Retail Controller. For the Longs retail operations, the valuation of real property (\$937.2 million) and personal property (\$229.3 million) was unchanged from the schedules sent on December 23. The Retail Controller forwarded the schedules to the Controller and to CVS’s outside auditors.

16. Also on January 13, CVS’s outside auditors told the Retail Controller that they wanted to have “a quick wrap up call this morning on the Longs valuation just to make sure we are all on the same page and close down our procedures. We wanted to talk about the wrap up process [and] timing of [the] narrative from [the valuation firm] etc.”

17. As of mid-January, the valuation firm was not performing any additional valuation work, and both the Retail Controller and CVS’s outside auditors expected that the firm would submit its report in time for inclusion in the 2008 audit.

18. On January 27, the valuation firm submitted a draft report that applied the “continued use” valuation premise mandated in the engagement letter (except for the stores to be closed). The valuation of the Longs drugstores had not changed from the draft schedules sent on December 23 and January 13: \$937.2 million of real property and \$229.3 million of personal property. The draft report was the “Phase Two” narrative report required by the engagement letter.

19. Between November 2008 and January 27, 2009, CVS and its outside auditors were in regular communication with the valuation firm about its work. At no point did CVS or the outside auditors express any concerns about the valuation firm’s approach to the valuation. Nor did CVS tell the valuation firm about any plans to dispose of almost all personal property in most Longs stores, despite the firm’s specific request for information about “future use / development / refurbishment projects at existing stores.” As a result, the valuation firm assumed that the conversion of Longs stores to CVS stores would primarily entail a change of signage.

20. After submitting its draft report on January 29, the valuation firm waited for comments from CVS's outside auditors so it could prepare its final report. On January 30, the Retail Controller told the firm: "[The auditors] completed their review of the draft valuation report and had no comments. Please issue your report in final form as soon as you can." The firm responded that it would send a draft management representation letter for CVS to sign, as well as "a final invoice for our work."

21. On January 31, the Retail Controller told the valuation firm to put finalizing the valuation report "on hold" in light of an upcoming meeting between the firm and the CVS real estate group.

22. On February 2, a manager in the CVS real estate group sent the valuation firm a list of topics to be discussed on a call later that day. Most of the topics concerned the accounting for leasehold interests and personal property in Longs stores to be closed. None of the topics concerned the remodeling of any Longs stores.

23. On February 11, the valuation firm sent CVS a "final summary" of the Longs valuation. The personal property in the Longs drugstores was still valued at \$229.3 million.

24. In connection with the year-end 2008 audit, CVS's outside auditors reviewed the valuation firm's approach to valuing tangible assets and concluded that the firm's methodology was reasonable. While the outside auditors were working on the 2008 audit, CVS did not disclose anything about its plans to remodel any Longs stores, and so the auditors did not review the Longs valuation report for any potential impact of the remodeling.

25. CVS included the values from the January 29 draft valuation report in its audited financial statements for 2008, which were included in its annual report to shareholders for 2008 and were incorporated by reference in the annual report on Form 10-K that it filed with the Commission on February 27. Note 2 to the audited financial statements, entitled "Business Combinations," indicated that CVS had acquired Longs for approximately \$2.6 billion. Note 3, entitled "Goodwill and Other Intangibles," stated that "goodwill increased primarily due to the Longs Acquisition" and that the increase in amortizable intangible assets "was primarily due to the preliminary purchase price allocations (which may change and the result of such changes, if any, may be material)." The audited financial statements did not contain any indication that the valuation of Longs tangible assets such as personal property was not final.

26. The asset values from the January 29 draft valuation report were loaded into CVS's books and records, and CVS began taking depreciation on the Longs assets.

27. On February 27, the Real Estate Finance Director asked the valuation firm about potential adjustments to the value of assets in the Longs stores to be closed. He also wrote:

Plus, it seems there have been several changes in individual store strategies over the past few weeks, and I would guess these have not been picked up by you guys or [the Retail Controller]. I would like to talk about how these changes and future changes should be handled with respect to these value adjustments.

Minutes later, a Senior Manager at the valuation firm responded with a warning:

[K]eep in mind that any changes in strategy that were not known as of the acquisition date cannot be reflected in the valuation. The valuation was as of October 30, 2008. So the valuation can only reflect the strategies in place at that time – which I believe we accurately reflected. Any changes after the valuation date would have to be discussed with your audit team.

28. The valuation firm did not perform any further work on the Longs valuation between February and April, although it responded to occasional questions from CVS.

Daniels Persuaded the Valuation Firm to Reduce its Valuation of the Longs Stores' Personal Property by \$189 Million

29. In March 2009, the CVS fixed asset group adjusted the depreciation being taken on Longs FF&E and technology assets by lengthening the remaining useful lives beyond the time period that the valuation firm had used. In other words, the fixed asset group assumed that these assets in the Longs stores would remain in use for a longer period than the valuation firm had assumed.

30. In April, the CVS property accounting group identified a discrepancy between the depreciation on Longs assets built into the 2009 budget and the actual depreciation being taken on those assets. On April 30, the Controller complained to the Retail Controller and to Daniels, who was then Vice President for Corporate Budgeting, that the CVS fixed asset group had apparently made decisions about the remaining useful lives of Longs assets that were inconsistent with the valuation firm's draft report, and the result was an unfavorable variance of \$20 million per month.

31. In early May, the Controller fired the Retail Controller. Daniels became the Retail Controller and took charge of working with the valuation firm on the Longs valuation. (At the time, the Controller was being scrutinized by CVS senior management as a possible successor to the CFO, who had expressed his intent to retire.)

32. On May 1, the Controller and Daniels asked for a conference call with the valuation firm on May 8. On May 7, Daniels prepared a list of four topics for the call: (1) a request for a summary schedule listing each asset class and the remaining useful lives; (2) a discussion of any recent changes in the valuation; (3) a discussion of the fair value and remaining useful lives for the "technology" assets; and (4) an apparent discrepancy in the labeling in two versions of the valuation schedules. The list did not mention the remodeling of any Longs stores or the disposal of any Longs assets. The Controller forwarded the list to the valuation firm.

33. As of May 8, the Controller had no concerns about the valuation of Longs drugstore assets or the projected depreciation on those assets.

34. After the call on May 8, the valuation firm sent Daniels its latest fixed asset valuation figures and the depreciation and amortization schedules that it had used. There had been no change to the \$229.3 million valuation of personal property in the Longs retail operations.

35. On May 11, after reviewing the materials he received from the valuation firm on May 8, Daniels told the Controller that: (1) the blame for the depreciation variance lay with the fixed asset group; (2) the valuation firm's estimated fair values and suggested remaining useful lives were the same as used by CVS in its current budget; and (3) the depreciation variance problem would likely be resolved in the financial results for April 2009.

36. At no point between January 27 and May 13 did CVS tell the valuation firm about any plans to dispose of almost all of the Longs stores' personal property, despite the firm's specific request for such information back in November 2008.

37. On May 13, Daniels told the valuation firm during a conference call that:

a. CVS was remodeling the Longs stores that were going to be operated for the long-term, and as part of the remodeling process, CVS was gutting the stores and discarding all the personal property; and

b. CVS was not receiving any value for the assets being discarded.

Daniels also told the valuation firm that, as of the acquisition date on October 20, 2008, CVS had intended to throw out all that personal property in the Longs stores.

38. On May 19, a Senior Manager at the valuation firm warned Daniels that it appeared CVS was improperly changing its real estate strategy after the acquisition date:

I had the opportunity to discuss our call from last week with [name omitted]. [He] is the partner in charge of the tangible asset valuation practice in the US and was the tangible asset partner on the CVS engagement. We discussed many of the changes in the plans for the PP&E [property, plant and equipment] that have occurred since the acquisition. [The valuation firm] valued the PP&E as of the acquisition date utilizing the plans of CVS at this time. The valuation of the PP&E cannot be modified for changes in plans that occurred after the valuation date. The future plans of the company had to be known prior to the acquisition date. Any changes that have occurred over the last 7 months that were not known as of October 30, 2008 cannot be incorporated into the valuation.

One hour later, Daniels sent an email to allay the valuation firm's concerns:

As a reminder, what we would like to discuss is the assumptions used regarding the intended use of the assets to ensure that the correct plans were used. Rest assured we are not looking to change the plans regarding the use of the acquired assets as the plans remain unchanged since the close. Rather, we want to make sure the correct assumptions were used.

39. Also on May 19, the partner responsible for the valuation firm's overall relationship with CVS reported on a call with Daniels:

He said he understands the acctg [accounting] literature and believes that we were given incorrect info. He said they hadn't really looked at our final report until after March when the info that was loaded into their g/l [general ledger] didn't look right.

40. On May 20, Daniels told a co-worker that he was working with the valuation firm “to ensure their valuation assumptions are correct.”

41. On May 26, Daniels had a conference call with the valuation firm. Prior to the call, Daniels provided the firm with CVS's current real estate strategy for the Longs stores. The strategy list indicated that CVS planned to: (1) close 71 stores within one year; (2) operate 124 stores with the intent to relocate them within three years (if possible); and (3) operate 333 stores for the long-term. Daniels also sent the firm an overview of the store remodeling project. The remodel overview indicated that 420 stores would be remodeled to some extent, of which 361 stores would receive a “full remodel.” (The stores not being remodeled at all were stores that had been or were about to be closed, as well as stores in Hawaii that were going to retain the “Longs” name.). The remodel overview indicated that less than one-third of the “full remodel” stores were going to receive all-new fixtures. However, Daniels told the valuation firm that all assets in all 361 “full remodel” stores were being scrapped.

42. The valuation firm's internal manual on SFAS 141 stated that PPA adjustments are appropriate only if “the necessary information was determinable at the time the preliminary allocation was reported,” as when, for example, the acquiring entity has commissioned an appraisal of plant and equipment that is not complete by the acquisition date.

43. The valuation firm accepted Daniels' statements in May that, as of the acquisition in October 2008, CVS intended to throw out personal property in the stores to receive a “full remodel,” and that CVS's failure to provide the firm with the correct information for six months after the firm was retained was due to a “miscommunication.” If the valuation firm had received this information before it submitted its draft report in January 2009, the fair value of the Longs drugstore assets would have been significantly reduced.

44. On June 3, the valuation firm told Daniels that the personal property in the Longs drugstores was now valued at \$49.6 million (compared with \$229.3 million as of May 8). The firm reduced the value of personal property by \$179.7 million based on the supposedly correct information provided by Daniels in May – that, as of the acquisition date on October 20, 2008, CVS intended to discard the assets in the stores to be remodeled, and that the discarded assets had no liquidation value.

45. On June 4, Daniels received a copy of the outside auditors' internal manual on SFAS 141R.³ The manual stated:

The measurement period ends once the acquirer is able to determine that it has obtained all necessary information that existed as of the

³ SFAS 141R expanded the subjects that can be modified during the allocation period but did not change the definition of the allocation period itself.

acquisition date or has determined that such information is unavailable...

Once the acquirer obtains the information it has arranged to obtain or determines that the information does not exist, then the measurement period is closed. The measurement period is not a fixed twelve-month period during which all changes in carrying values of assets acquired or liabilities assumed are considered adjustments to the business combination accounting.

46. On June 16, Daniels told a co-worker, “Wanted to give you a quick update on the Longs valuation. We have made some good progress on the tangible asset side based on having [the valuation firm] update their assumptions to include the correct real estate disposition and intended use of the assets.”

47. On July 28, the valuation firm sent Daniels an “updated draft” of its valuation report. The text of the report had not changed since the January 27 draft, but the value of personal property in the Longs drugstores had been reduced from \$229.3 million to \$50.8 million.

48. On October 1, the valuation firm sent Daniels a “final draft” of its valuation report. The text of the report had not changed since the draft sent on July 28. However, the value of personal property in the Longs drugstores had been further reduced – from \$50.8 million to \$39.6 million. The total reduction in the value of personal property in the Longs drugstores since the firm’s January 27 draft report was approximately \$189 million (from \$229.3 million to \$39.6 million).

CVS’s Outside Auditors Accepted the \$189 Million Reduction in the Valuation of the Longs Stores’ Personal Property

49. Until the spring of 2009, CVS’s outside auditors were not aware that CVS planned to discard almost all of the Longs stores’ personal property.

50. In early June 2009, Daniels told the outside auditors that CVS had finalized its strategy for which Longs stores would be closed, relocated or remodeled, and that the adjustments to the valuation of the Longs stores could be larger than expected, because CVS was going to scrap all personal property in the stores being remodeled. That was the first time the outside auditors heard about the write-off of assets in stores being remodeled. The Coordinating Partner told the Engagement Partner that he was a “little worried about what he [Daniels] may be trying to do.”

51. On June 19, Daniels told a member of the Longs remodeling team at CVS:

I’m close to completing the valuation work with [the valuation firm] for Longs. One final step I have is getting our auditors comfortable with the changes. Our auditors were hoping they could see a summary of what we are spending on the resets [remodels] that have been completed. Is it possible to get a summary (with some detail) for the 4 stores that are done? Since we are writing off a lot of the assets they

would feel more comfortable seeing that we're spending a fair amount per store to reset them.

52. On September 25, the Manager of Property Accounting provided Daniels with a spreadsheet listing the amount spent on remodeling: (1) each Longs location whose assets had been written down to zero, and (2) each Longs location whose assets were included in the residual valuation of \$50 million:

You had asked me to compare the Long's Personal Property acquisition assets that retained their value (\$50M) following the recent revaluation, to the total spending for the Long's Reset capital projects. This analysis is attached.

As you can see on the "Summary" tab, the theory you outlined to me holds true for the majority of the stores. Those stores that have retained-value acquisition assets generally have lower levels of spending on their Reset projects. Conversely, those locations that have significant Reset spending generally do not have large acquisition asset activity. There are exceptions, of course, but in general the attached information supports your position.

53. The language in these emails is very revealing. Daniels asked for data about "reset spending" at the Longs stores to help the outside auditors get "comfortable" because CVS was "writing off a lot of the assets." He did not ask for confirmation that CVS was actually scrapping all personal property in the stores being remodeled. The Manager of Property Accounting told Daniels that, "for the majority of the stores," the data supported "the theory you outlined to me" and that "in general the attached information supports your position." The "theory" and "position" which Daniels had outlined to him was simply that stores with lower retained asset values tended to have more "reset spending" – not that all assets in the "full remodel" stores were actually being discarded.

54. On October 5, the outside auditors' Senior Manager alerted others members of the audit team about the upcoming finalization of the Longs PPA:

The biggest change is that PP&E went from 229 million in the initial valuation to 50 million (and in final one expected to be 39 million).

The reason behind this as it has been explained to us is that CVS was either resetting / relocating / closing a number of the stores that was never communicated to [the valuation firm] and therefore an asset value was assigned that was way too high.

55. On October 8, after the valuation firm had further reduced the valuation of the remaining Longs store assets to \$39 million, the Manager of Property Accounting sent Daniels an updated store-by-store spreadsheet reflecting a total of \$97 million of "reset [remodeling] project" spending and \$225 million of "post-acquisition" spending. Daniels forwarded the spreadsheet to the outside auditors.

56. On October 14, the valuation firm's Senior Manager provided Daniels with answers to questions from the outside auditors about the revised valuation. In response to the auditors' request for clarification about the adjustments to personal property, the Senior Manager wrote:

We were provided an updated strategy list from CVS that contained a future plan for each store. Below is a synopsis of how we valued the personal property for each strategy.

Remodel – We were informed that stores that were being remodeled from a Long's to a CVS were being gutted and the personal property was being scrapped. CVS was not obtaining any residual value for these assets as they were being discarded. Therefore the personal property at stores that were undergoing a complete renovation to a CVS were given no value (scrap = \$0).

Closed Stores – All stores that were closed were being gutted and none of the personal property was being retained by CVS. The personal property was valued at \$0.

Closing Stores – Stores that would be operated for less than 1 year and then closed – We valued the personal property with a 1 year RUL [remaining useful life]. The depreciation was accelerated so that the personal property would be fully depreciated at the end of 1 year.

Stores that were being converted to CVS for long term use and underwent minor cosmetic changes – We valued the personal property in continued use and the signage at \$0.

Daniels forwarded the valuation firm's response to the outside auditors.

57. Daniels never provided the outside auditors with any documents specifically confirming that CVS was gutting all the "full remodel" stores. Instead, when they accepted the PPA adjustments, the outside auditors relied on: (1) the representations by Daniels that CVS had always intended to scrap all assets in the Longs stores to be remodeled; and (2) the data identifying the amount of capital expenditures at each store.

CVS's Form 10-Q for the Third Quarter of 2009 Included Adjustments to the Longs PPA

58. On November 5, CVS filed a Form 10-Q with unaudited financial statements for the third quarter of 2009 that included adjustments to the Longs PPA.

59. Compared to the valuation firm's January 2009 draft report, the value of Longs tangible assets was reduced by \$212 million and goodwill was increased by the same amount. The reduction of tangible assets resulted primarily from the \$189 million decrease in the value of personal property in the Longs drugstores reflected in the firm's "final draft" valuation report dated October 1.

60. CVS made a one-time catch-up adjustment by reversing \$49 million of the depreciation taken on Longs assets from the closing in October 2008 through June 2009. In addition, CVS did not take \$19 million of depreciation that would otherwise have been taken on Longs assets in the third quarter.

61. The \$49 million one-time depreciation reversal increased third-quarter 2009 EPS by 2.4¢.

Daniels Caused CVS to Make Improper Accounting Adjustments

62. Daniels told a co-worker on June 16, 2009 that he had been making “some good progress on the tangible asset side” with the valuation firm and that he was now “extremely confident (by the way that’s the most confident I get) that the final valuation will no longer be a bad guy but rather a good guy.”

63. Some of Daniels’ statements to the valuation firm and the outside auditors are inconsistent:

a. Daniels told the valuation firm on May 19 that no one at CVS had really looked at the January 27, 2009 draft report until after March, and that CVS became worried about the valuation only when the values that were loaded into its general ledger “didn’t look right.” However, Daniels told the Controller earlier in May that the valuation firm’s estimates of fair value and suggested remaining useful lives were the same as used by CVS in its current budget.

b. Daniels told the valuation firm and the outside auditors on several occasions that CVS had not provided the valuation firm with the correct plans for the Longs stores. However, on September 28, Daniels told the Controller that the PPA adjustments should not be considered as the correction of an error:

[W]e don’t fall under this scenario in my opinion as the r/e [real estate] strategy was still being worked on, thus we didn’t ignore available info resulting in an error. Rather we were waiting to gather info to complete the valuation in the first place.

64. More importantly, the facts fatally undermine Daniels’ justification for the PPA adjustments –that, as of the acquisition date on October 20, 2008, CVS intended to scrap all assets in the Longs stores to be remodeled.

65. When CVS acquires a chain of drugstores, it typically tries to reuse as many assets as possible, and it makes a store-by-store determination about the ultimate disposition of the assets. When it acquired the Longs stores in October 2008, CVS did not know what its remodeling plan was going to be or which assets in the stores to be retained would have value. As a result, it took months after the acquisition for CVS to develop its plans for remodeling the Longs stores.

66. On October 17, 2008, the CVS real estate group circulated a “Longs Integration Update” indicating that CVS would “update the look of the Longs’ fleet of stores” with “CVS Decor Elements – Graphics, Aisle Guides, Carpet, Paint etc.” The document contained numerous

references to the minimization of construction costs, the retention of many existing fixtures, and the need to finalize the scope of work.

67. On January 6, 2009, a member of the CVS real estate group circulated a brief comparison between the company's plans for the Longs stores and its treatment of the Albertsons stores that CVS had acquired a few years earlier:

LDG [Longs]: Retain major elements from Longs > Total Visual Appeal (TVA) Remodel store program.

ABS [Albertsons]: All new CVS design.

Benefit: Reduced cost while adding CVS look and feel elements (e.g. aisle markers, graphics, carpet etc).

68. On January 29, members of the Longs integration team reported on a site visit to a model "Alpha" store that had been built in an empty location to assess possible interior design elements for the remodeled Longs stores. The report included several suggestions for how to adapt to the taller shelving in a Longs store and how to respond to customer feedback.

69. On February 13, members of the Longs integration team submitted a report on the "Alpha" store that included "reusing existing fixtures where possible, even if not standard for CVS."

70. On February 19, the CVS real estate group circulated a proposed budget of \$202 million for the Longs store remodeling project. For the 419 stores to be remodeled, the report identified five levels of work, running from the "A+ scope" costing \$640,000 per store to the "C scope" costing \$67,000 per store. Another presentation of the proposed budget noted that "the following areas drive the costs: 1) photo/checkout; 2) former cosmetic service areas; 3) carpets." There was no reference to the complete replacement of all fixtures in all remodeled stores.

71. On May 1, members of the Longs integration team reported on lessons learned from the five "Beta" stores built in March. The report mentioned potential changes to the store design and concluded, "Save tens or hundreds of thousands of dollars by keeping some existing elements."

72. On May 22, the CVS real estate group circulated a "Longs Remodel Overview" indicating that 420 stores were being remodeled to some extent. 361 stores would receive a "full remodel" that included:

New CVS checkout: this will require the removal of 1 or 2 grocery style checkout lanes;

New CVS Photo Lab: this will require the removal of the existing Longs photo lab in order to accommodate the CVS design;

New Graphics/Wayfinding: all existing Longs department and merchandise graphics will be replaced with the standard CVS package;

New exterior signage: replacement of existing Longs banner with CVS/pharmacy.

The overview indicated that, despite the nomenclature, only 111 of the 361 “full remodel” stores (fewer than one-third) were going to receive “replacement of existing wall and gondola fixtures.”

73. Although it did not involve the gutting of all stores to be operated for the long-term, the final remodeling plan was more extensive than either CVS or its outside auditors had initially expected.

The Longs PPA Adjustments Did Not Comply with GAAP

74. Under SFAS 141 (“Business Combinations”), an acquiring entity should allocate the cost of the acquired entity to the assets and liabilities assumed “based on their estimated fair values at [the] date of acquisition.” [¶35.] “Plant and equipment” should be valued at “current replacement cost ... unless the expected future use of the assets indicates a lower value.” [¶37d(1).]

75. Under SFAS 141, an “allocation period” may be needed “to identify and measure the fair value” of the assets and liabilities. [Appendix F.] The allocation period “is intended to differentiate between amounts that are determined as a result of the identification and valuation process ... and amounts that are determined because information that was not previously obtainable becomes obtainable.” [¶B183.] The allocation period “ends when the acquiring entity is no longer waiting for information that it has arranged to obtain and that is known to be available or obtainable.” [Appendix F.] In other words, a PPA adjustment is valid only if it is based on information that the acquiring entity “has arranged to obtain” and that was “known to be available or obtainable” on the acquisition date.⁴

76. Under SFAS 141, CVS could only make adjustments to the Longs PPA based on information that was known or knowable as of the acquisition date on October 20, 2008. Given the facts set forth above, the PPA adjustments in the third quarter of 2009 (writing off \$189 million of personal property in the Longs stores) were not proper under SFAS 141 because:

- a. They did not reflect CVS’s intended future use of those assets as of the acquisition date on October 20, 2008;
- b. They did not reflect information that was known or knowable to CVS as of October 20, 2008; and
- c. They did not account for CVS’s use of the assets to generate revenue after October 20, 2008.

77. The conclusion that the write-off of assets supposedly discarded during the remodeling process should not have been treated as a PPA adjustment is consistent with CVS’s

⁴ See also Staff Accounting Bulletin No. 103 (“The staff believes that the allocation period should not extend beyond the minimum reasonable period necessary to gather the information that the registrant has arranged to obtain for purposes of the estimate.”).

prior acquisitions, in which: (1) CVS did not write off the assets in stores being remodeled; and (2) subsequent decisions about which stores to close (not which stores to remodel) were the primary reason for changes to the PPA.

78. Under SFAS 144 (“Accounting for the Impairment or Disposal of Long-Lived Assets”),⁵ if CVS really had discarded \$189 million of personal property in the third quarter of 2009, it should have:

a. Written off \$140 million of net book value (the original \$189 million minus the \$49 million of depreciation to date) as an expense in the period in which it stopped using the assets; and

b. Left the \$49 million of previously recorded depreciation unchanged.

79. With proper accounting, current-period expenses in the third quarter of 2009 would have been as much as \$189 million higher than was actually reported. For the quarter, the failure to recognize as much as \$189 million of current-period expenses overstated operating profit by as much as 13.7%, overstated income from continuing operations by as much as 12.5%, overstated net income by as much as 12.5%, and overstated EPS by as much as 17% (as much as 9.3¢).

Violations

80. As a result of the conduct described above, Daniels:

a. Violated Section 17(a)(2) and (3) of the Securities Act, which prohibits making untrue or misleading statements of material fact or engaging in conduct which operates or would operate as a fraud or deceit upon the purchaser in the offer and sale of securities. Sections 17(a)(2) and 17(a)(3) do not require a showing of scienter. *Aaron v. SEC*, 446 U.S. 680, 697 (1980);

b. Violated Rule 13b2-1 promulgated under the Exchange Act, which prohibits any person from directly or indirectly falsifying any books and records subject to Section 13(b)(2)(A) of the Exchange Act;

c. Aided and abetted and caused CVS’s violations of Section 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder, which require an issuer to file accurate quarterly reports with the Commission and require those reports to contain such further material information as is necessary to make the required statements in the reports not misleading;

d. Aided and abetted and caused CVS’s violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act, which require an issuer to make and keep books and records that accurately and fairly reflect the dispositions of its assets, and to devise and maintain a system of internal accounting controls sufficient to ensure that its transactions comport with Generally Accepted Accounting Principles; and

⁵ FASB statements were codified for all interim periods ending after September 15, 2009. SFAS 144 has been codified as ASC 360, *Property, Plant and Equipment*.

e. Pursuant to Rule 102(e)(1)(iii) of the Commission's Rules of Practice, willfully violated Section 17(a)(2) and (3) of the Securities Act and Rule 13b2-1 promulgated under the Exchange Act, and also willfully aided and abetted and caused CVS's violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder.⁶

Findings

81. Based on the foregoing, the Commission finds that Daniels: (a) willfully violated Section 17(a)(2) and (3) of the Securities Act and Rule 13b2-1 promulgated under the Exchange Act; and (b) willfully aided and abetted and caused CVS's violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder.

IV.

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

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

A. Daniels shall cease and desist from committing or causing any violations and any future violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act, and Rules 12b-20, 13a-13, and 13b2-1 thereunder and Section 17(a) of the Securities Act.

B. Daniels is denied the privilege of appearing or practicing before the Commission as an accountant, pursuant to Rule 102(e)(1)(iii) of the Commission's Rules of Practice.

C. After one year 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

⁶ As used in these findings, a willful violation of the securities laws means merely "that the person charged with the duty knows what he is doing." *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C. Cir. 1949)).

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.

D. 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.

E. Respondent shall, within 10 days of the entry of this Order, pay a civil penalty in the amount of \$75,000 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717. Payment must be made in one of the following ways: (1) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or (2) Respondent may pay by certified check, bank cashier’s check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Laird Daniels as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to John T. Dugan, Associate Regional Director, Boston Regional Office, Securities and Exchange Commission, 33 Arch Street, Boston, MA 02110.

By the Commission.

Jill M. Peterson
Assistant Secretary