OFFICE OF INSPECTOR GENERAL

Federal Housing Finance Agency

400 7th Street, S.W., Washington DC 20024

DATE:	May 3, 2013
TO:	Edward J. DeMarco, Director (Acting)
FROM:	Steve A. Linick, Inspector General
SUBJECT:	Public Company Auditing Oversight Board Criticisms of Public Accounting Firms that Do Business with the GSEs

I am bringing to your attention the fact that the federal regulatory organization responsible for oversight of firms conducting audits of public companies in the United States has been publicly critical of past audit work conducted by public accounting firms engaged to perform audits of the housing Government-Sponsored Enterprises (GSEs).

The Public Company Accounting Oversight Board (PCAOB or the Board) is a nonprofit corporation established by Congress, pursuant to the Sarbanes-Oxley Act of 2002 (the Act), to oversee the audits of public companies in order to protect investors and the public interest by promoting informative, accurate, and independent audit reports. The Securities and Exchange Commission (SEC) has oversight authority of the Board, including the approval of the Board's rules, standards, and budget.

The Board inspects selected audit work of registered public accounting firms to assess compliance with the Act, the rules of SEC and the Board, and professional standards. The Board is required to conduct those inspections annually for firms that regularly provide audit reports for more than 100 public companies, and at least triennially for firms that regularly provide audit reports for 100 or fewer public companies.

PCAOB Guidance Issued on Public Disclosures

On August 26, 2004, the PCAOB issued as a release (No. 104-2004-001) a statement concerning the issuance of inspection reports.[1] The release provided information concerning the inspection report process and the public availability of information in the reports. The statement explains that "[i]n the context of an inspection report, the Board generally will maintain as nonpublic any otherwise nonpublic information that the Board obtained concerning the firm or its clients (except where disclosure is incident to disclosure of a quality control defect that the firm has not addressed to the Board's satisfaction)." In addition, the release explains that if a violation of law, Board rules, SEC rules, or professional standards is established, that information will

[1] Available at http://pcaobus.org/Inspections/Documents/Statement_Concerning_Inspection_Reports.pdf.

become public through the appropriate disciplinary and enforcement processes. Nonpublic content includes a discussion of potential defects in an audit firm's system of quality control. Such quality control criticisms remain nonpublic if the firm satisfactorily addresses them within 12 months of the report date.

PCAOB Guidance Issued for Audit Committees

In August 2012, the PCAOB released a memorandum entitled "*Information for Audit Committees About the PCAOB Inspection Process*." The memorandum explains that the PCAOB cannot disclose to the audit committee the nonpublic portion of an inspection report or other nonpublic inspection information – including whether the inspection identified deficiencies in the audit that the audit committee oversees. Furthermore, the PCAOB cannot require an audit firm to disclose such information to an audit committee. However, the memorandum states that audit committees might wish to review PCAOB inspection reports with their audit firm and discuss the results with the firm. The memorandum contains sample questions that an audit committee might ask their audit firms after a PCAOB inspection.

Board Criticisms Made Public

The Board has publicly released adverse information concerning public accounting firms that are used by the housing GSEs. For example, on October 17, 2011, the Board publicly disclosed audit deficiencies identified at Deloitte & Touche LLP (D&T) during its 2007 inspection of that firm. D&T is a public accounting firm that conducts the annual financial statement audits of Fannie Mae.

On March 7, 2013, the Board publicly released adverse information from inspection reports of PricewaterhouseCoopers (PwC), the public accounting firm that conducts the annual financial statement audits of Freddie Mac and all 12 Federal Home Loan Banks. Specifically, the Board made public certain criticisms of PwC for audit years 2008 and 2009 because PwC had not satisfied the Board's concerns within the 12-month remediation periods.[2] The Board's unresolved concerns with regard to PwC's audit work included the areas of:

- Professional skepticism and due care
- Supervision and review
- Reliance on controls
- Use of the work of others
- Estimates and fair value measurements

[2] PCAOB's public reports can be found at http://pcaobus.org/Inspections/Pages/default.aspx.

OIG Concerns

The GSEs regularly do business with public accounting firms subject to PCAOB oversight and inspection. It is my understanding that GSE audits were not part of the deficiencies identified by the Board at D&T and PwC. Nevertheless, my office met with FHFA's Chief Accountant on March 14, 2013, to discuss the PwC matter. The Chief Accountant appeared to be aware of the issue and has been in communication with affected parties, including the GSEs. He expressed confidence that awareness of the issue is high among the GSE audit committees. Additionally, the Chief Accountant and FHFA examiners meet regularly with public accounting firms to discuss various audit issues and have reportedly discussed the results of the PCAOB inspections at length.

While FHFA's awareness and monitoring of the PwC matter is notable, we recommend that FHFA request that Fannie Mae, Freddie Mac, and each FHLBank provide FHFA with confirmation that their audit committees and management are providing elevated attention to audit quality at D&T and PwC and the specific steps being taken.

Looking forward, such information may prove useful for supervisory purposes and, in the case of Fannie Mae and Freddie Mac, conservatorship oversight.

Please let me or Russell Rau, Deputy Inspector General for Audits, know if you would like to further discuss this matter.

cc: Jon Greenlee, Deputy Director, Division of Enterprise Regulation
Fred Graham, Deputy Director, Division of Federal Home Loan Bank Regulation
Nina Nichols, Deputy Director, Division of Supervision Policy and Support
Jeffrey Spohn, Deputy Director, Office of Conservatorship Operations