



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 Accounting 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



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DATE: July 31, 2013

TO: Steve A. Linick, Inspector General

FROM: Nicholas Satriano, Chief Accountant 

SUBJECT: Public Company Accounting Oversight Board (PCAOB) Criticisms of Government-Sponsored Enterprises (GSEs) Audit Firms

Acting Director Ed DeMarco asked that I respond to your memo on the PCAOB criticisms of the GSEs' audit firms. In response to your suggestion for the Federal Housing Finance Agency (FHFA) "to request that Fannie Mae, Freddie Mac, and each Federal Home Loan Bank (FHLB), provide FHFA with confirmation that their audit committees and management are providing elevated attention to audit quality at PricewaterhouseCoopers (PwC)¹ and Deloitte & Touche (D&T)," outlined below are the steps that were taken by the GSEs Audit Committees, management, and FHFA. Please note, FHFA was engaged with the GSEs on this issue prior to receiving your memo.

Ongoing Efforts

Annually, the Board of Directors of each GSE is required to assert to FHFA its compliance with FHFA's Examination Guidance for Accounting Practices. This guidance is designed to promote safe and sound accounting practices including, but not limited to: policy and procedures, systems, reporting and disclosure. One of the requirements is to report on compliance with "*a report by the external auditor describing in detail the auditing firm's internal quality-control procedures; any issues raised by the most recent internal quality-control review, peer review, or PCAOB inspection of the firm and any steps taken to deal with any such issues, including the auditing firm's letters of responses to the peer review and PCAOB inspection reports. The Chief Accountant may meet with senior partners or representatives of the auditing firm to discuss the report by the independent auditor, peer review report, or PCAOB inspection report and various letters of response in understanding the firm's quality control procedures.*" The 2012 reports, which were due June 30, 2013, have been received for Fannie Mae, Freddie Mac and all of the FHLBs.

¹ PwC is responsible for the Freddie Mac audit engagement and each of the twelve FHLBs as well as the Office of Finance. D&T is responsible for the Fannie Mae audit engagement.

As a matter of course, annually, both the PwC and D&T audit engagement partners review the results of their annual PCAOB inspection report and remediation efforts underway with the GSEs Audit Committees and management.

Monthly or as necessary, we meet with PwC and D&T on accounting and auditing matters related to the GSEs. As applicable, this includes a discussion and review of the PCAOB inspection reports, peer reviews, and other items. Staff well versed in the GSEs and the subject matter criticisms raised by the PCAOB participate in these meetings. FHFA met with both PwC and D&T regarding the public release of their inspections reports to understand the conclusions and actions taken by the firms.

In November 2012, PwC disclosed to the Audit Committee and management of Freddie Mac the possibility that the PCAOB may release the non-public portion of its inspection report for the years 2008 and 2009. In December 2012, PwC made a special presentation to the Audit Committee and management on the PCAOB inspection process, findings, and steps taken by PwC to enhance its quality controls. In March 2013, the PCAOB released the non-public portion of its inspection report for these years.

Subsequent to the release of the non-public findings by the PCAOB, PwC provided Freddie Mac's Audit Committee and management a summary of each quality control criticism noting the specific relevance to the Freddie Mac engagement and the quality control measures in place to ensure these criticisms would not apply had the PCAOB reviewed the Freddie Mac engagement. In addition, the Audit Committee and management evaluated the existing controls and procedures to ensure they are designed and operating effectively. The Audit Committee and management concluded that the risks associated with the quality control criticisms identified in the non-public portion of the report have been mitigated by changes introduced by PwC in response to the report, and strong internal controls and governance in place at Freddie Mac.

With respect to the FHLBs, PwC leadership briefed the FHLBs Audit Committee Chairpersons in late October 2012 about the future release of the non-public findings of the PCAOB inspection reports, the nature of the criticisms and actions the firm had taken to address these items. In March 2012, PwC leadership had multiple briefings with all Audit Committee Chairpersons, as well as with each FHLBs Audit Committee on the non-public information from the PCAOB report. These briefings also covered remediation efforts and the implications to the FHLBs and individual audits. None of the FHLB engagements were reviewed as part of the PCAOB inspection.

The Audit Committees of Freddie Mac and the FHLBs have submitted documentation supporting their efforts responding to the criticisms by the PCAOB of PwC. We believe the actions taken by Freddie Mac and the FHLBs Audit Committees are appropriate and indicative of the GSEs commitment to ensuring audit quality.

In October 2011, the PCAOB released non-public findings from the 2007 inspection report for D&T. At the time, the Audit Committee, management and FHFA reviewed and evaluated the criticisms. Of note, in July 2011, the PCAOB selected the Fannie Mae engagement for inspection. The PCAOB had no findings related to this engagement.

Subsequently, we have requested that the Fannie Mae Audit Committee provide FHFA with formal documentation related to the Committee's review and evaluation of the release of the non-public portions of the PCAOB report released related to the 2007 inspection report.

Thank you for sharing your concern. Please let me know if you should have any further questions or comments.

cc: Mr. Edward DeMarco
Mr. Richard Hornsby
Mr. Jon Greenlee
Mr. Fred Graham
Ms. Nina Nichols