

United States Senate

WASHINGTON, DC 20510

March 21, 2023

Erica Y. Williams
Chair
Public Company Accounting Oversight Board
1666 K Street NW
Washington, DC 20006

Dear Chair Williams:

The collapse of Silvergate Bank, Silicon Valley Bank, and Signature Bank in the last several weeks have raised fresh concerns about the role of cryptocurrency's impact on the banking and financial systems, and extent to which investors, consumers, and banks are aware of these risks.

One particular concern is the role that shady audits play in giving crypto firms a veneer of safety and financial stability. We wrote to you about this matter earlier this year, raising concerns that PCAOB needed to rein in these shady audits.¹ Today, we write regarding your response to that letter, which revealed that PCAOB has not done enough to address these risks. In the wake of numerous bank failures, it is even more important that you take action to maintain investors', consumers', and banks' confidence in PCAOB-registered audit firms.

Your response confirmed that you are aware of the threats. You wrote that "I share your concern that when PCAOB-registered auditors perform "sham audits" – even for entities whose audits generally fall outside of our jurisdiction – there are risks to investors and the PCAOB,"² and that "use of digital assets presents unique audit risks to companies and requires an appropriate risks assessment and audit response by audit firms."³

And you specifically highlighted the threats from "Proof of Reserve" engagements by third party companies on behalf of auditors, writing that:

If a crypto firm were to attempt to pass off a PoR engagement as a PCAOB audit, then investors – particularly retail investors who may lack the experience and resources of institutional investors to protect themselves through other means – risk being misled that the limited comfort being offered through a PoR engagement is equivalent to the robust third-party assurance provided through a PCAOB audit, when in fact they are receiving none of those safeguards. As a result, investors may underestimate investment risk and make erroneous investment decisions to their potentially severe detriment.⁴

¹ Letter from Senator Elizabeth Warren to PCOB Chair Erica Williams, January 25, 2023, <https://www.warren.senate.gov/imo/media/doc/2023.01.25%20Letter%20to%20PCAOB%20re%20Crypto%20Audits.pdf>.

² Letter from PCAOB Chair Erica Williams to Sens. Warren and Wyden, Feb. 8, 2023, p. 1.

³ Letter from PCAOB Chair Erica Williams to Sens. Warren and Wyden, Feb. 8, 2023, p. 3.

⁴ Letter from PCAOB Chair Erica Williams to Sens. Warren and Wyden, Feb. 8, 2023, p. 6.

We are also pleased that, on March 8, 2023 – two days before the FDIC took over Silicon Valley Bank – the PCAOB’s Officer of the Investor Advocate put out a public warning about these proof-of-reserve reports, writing that:

The Office of the Investor Advocate is aware of some service providers, including PCAOB-registered audit firms, issuing proof of reserve reports (“PoR Reports”) to certain crypto entities ... Proof of reserve reports are inherently limited, and customers should exercise extreme caution when relying on them to conclude that there are sufficient assets to meet customer liabilities.⁵

These are important acknowledgments by PCAOB of the risks from crypto, and from PCAOB-registered auditors purporting to provide legitimate audits of crypto firms. But we continue to be disappointed by your unwillingness to use PCAOB’s existing authority to rein in these abusive practices by registered auditors.

Your response asserted that “the PCAOB faces statutory limits when it comes to regulating the audits of certain cryptocurrency companies ... As a general matter, audit firms registered with the PCAOB must follow PCAOB standards and rules specifically in connection with their audits of SEC-registered brokers or dealers only ... legislative changes would be needed for the PCAOB’s standard-setting, inspections, and enforcement programs to apply to audits and auditor behavior concerning entities that are not SEC-registered issuers, brokers or dealers.”⁶

A plain reading of the text of the Sarbanes-Oxley Act, which created the PCAOB and established its authority, clearly states that PCAOB has the authority to act on its broad responsibility to protect the integrity of the auditing system for SEC registered brokers, dealers, and issuers. And given that the ongoing use of sham audits of crypto firms conducted by PCAOB-registered auditors mislead the public and threatens the integrity of that auditing system – and we now know, potentially the banking and financial systems – you have both the authority and responsibility to rein them in.

The Sarbanes-Oxley Act contains language giving the PCAOB rulemaking authority over auditors that work for SEC-registered issuers, brokers, or dealers. Specifically, the law states that

The Board shall ... establish ... auditing, quality control, ethics, independence, and other standards relating to the preparation of audit reports for issuers, brokers, and dealers, in accordance with section 7213 of this title; ... [and] perform such other duties or functions as the Board ... determines are necessary or appropriate to promote high professional standards among, and improve the quality of audit services offered by, registered public accounting firms and associated persons thereof, or otherwise to carry out this Act, in order to protect investors, or to further the public interest.”⁷

⁵ PCAOB, “Investor Advisory: Exercise Caution With Third-Party Verification/Proof of Reserve Reports,” March 8, 2023, <https://pcaobus.org/resources/information-for-investors/investor-advisories/investor-advisory-exercise-caution-with-third-party-verification-proof-of-reserve-reports>.

⁶ Letter from PCAOB Chair Erica Williams to Sens. Warren and Wyden, Feb. 8, 2023, pp. 1-2.

⁷ 15 U.S. Code § 7211 - Establishment; administrative provisions, <https://www.law.cornell.edu/uscode/text/15/7211>.

Although these standards must be related to audit reports of SEC-registered issuers, brokers, and dealers, they are not required to be exclusive to them. If, as you concede, PCAOB-registered firms can fool investors by issuing sham audits⁸, then investors have no way of knowing when these auditors' work is worthy of their trust. If investors can be misled by, or cannot trust auditors' ethics and competence when it comes to their review of non-public companies, they can also be misled by, or may distrust audits or reviews for SEC-registered firms.

Auditors' sham reviews of crypto firms cast distrust and disrepute upon the entire auditing system: no credible auditor of public companies should be providing sham audits of crypto or other non-public firms. You have ample authority to establish standards for auditors that require any SEC-registered auditor to only conduct audits of crypto firms that comply with existing standards for audit quality. Based on the obvious threats to investors and the public interest posed by sham audits, any audits and reviews of crypto firms done by SEC-registered auditors must maintain a high level of scrutiny. Otherwise, these sham audits must be addressed by PCAOB.

Further, sham crypto audits may have serious implications for the broader financial system. FTX, the now-defunct crypto exchange which used customer deposits to fund risky investments at sister-company Alameda Research, received sham financial reviews by two PCAOB-registered auditors.⁹ FTX was a depositor at Silvergate Bank and Signature Bank, both of which failed, in part, due to excessive crypto exposure.¹⁰ In assessing the risks associated with the FTX's deposits, as well as those of other crypto-related customers, the banks may have relied on the misleading and faulty financial information provided by proof-of-reserve examinations. The continued production of proof-of-reserve reports, or any other financial review done by PCAOB-registered auditors that does not meet PCAOB standards, could introduce greater risk to our banking and financial system.

As the threats posed by crypto to banks and publicly traded firms and the financial systems become even more clear, it is critical that PCAOB use its existing authority to ensure that sham crypto audits do not become an even bigger threat to investors, the public interest, and the integrity of the accounting system for SEC-registered issuers, brokers, and dealers. We ask that you use this authority quickly – and that you provide us with answers to the following questions no later than April 4, 2023. We also ask that you provide us with a staff-level briefing on this matter no later than March 31, 2023.

⁸ Letter from PCAOB Chair Erica Williams to Sens. Warren and Wyden, Feb. 8, 2023, p. 1.

⁹ Financial Times, "FTX collapse puts auditors in the spotlight," Stephen Coley, November 13, 2022, <https://www.ft.com/content/930c6cea-5457-4dfa-9d47-666c0698c335>; Wall Street Journal, "FTX Tapped Into Customer Accounts to Fund Risky Bets, Setting Up Its Downfall," Vicky Ge Huang, Alexander Osipovich, Patricia Kowsmann, November 11, 2023, <https://www.wsj.com/articles/ftx-tapped-into-customer-accounts-to-fund-risky-bets-setting-up-its-downfall-11668093732>.

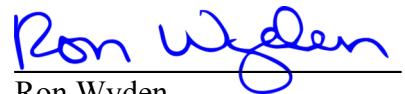
¹⁰ Bloomberg, "Silvergate Bet Everything on Crypto, Then It All Evaporated," Max Reyes, March 8, 2023, <https://www.bloomberg.com/news/articles/2023-03-09/silvergate-bet-everything-on-crypto-then-watched-it-evaporate>; New York Times, "Risky Bet on Crypto and a Run on Deposits Tank Signature Bank," Matthew Goldstein and Emily Flitter, March 12, 2023, <https://www.nytimes.com/2023/03/12/business/signature-bank-collapse.html>.

1. Do you believe that sham audits of crypto firms may have played a direct or indirect role in the collapse of Silvergate Bank, Signature Bank, or Silicon Valley Bank, and do you commit to investigating whether or not these audits did contribute to bank collapses?
2. To the extent that PCAOB-registered auditors are conducting sham audits or proof-of-reserve reports for crypto firms, what steps will PCAOB take to reduce the capacity these audits have to mislead investors and the public?
3. To what extent can these less-than-stringent audits or proof-of-reserve reports raise questions about the quality controls in place for auditing firms that conduct them?
4. To what extent can these less-than-stringent audits or proof-of-reserve reports raise questions about the ethics of auditing firms that conduct them?
5. To what extent can these less-than-stringent audits or proof-of-reserve reports raise questions about the independence of auditing firms that conduct them?
6. If SEC-registered auditors are conducting sham audits or proof-of-reserve reports for crypto firms, do you believe this raises questions about whether the audit firms are meeting “high professional standards” that they are required by law to meet?¹¹
7. If SEC-registered auditors are conducting sham audits or proof-of-reserve reports for crypto firms, do you believe this raises questions about the overall “quality of audit services offered by” these firms?¹²

Sincerely,



Elizabeth Warren
United States Senator



Ron Wyden
United States Senator

¹¹ 15 U.S. Code § 7211 - Establishment; administrative provisions,
<https://www.law.cornell.edu/uscode/text/15/7211>.

¹² 15 U.S. Code § 7211 - Establishment; administrative provisions,
<https://www.law.cornell.edu/uscode/text/15/7211>.