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April 19, 1978

CHAIRMAN'S OFFICE
RECEIVED

Honorable Harold M. Williams, Chairman
Securities and Exchange Commission
Washington, D. C. 20549

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Dear Mr. Chairman:

C. & EXCH. COMM.

This letter will serve a further interim report on the activities of the Public Oversight Board (POB) of the SEC Practice Section of the Division for Firms of the American Institute of Certified Public Accountants. As you know, the POB still has only three members, Messrs. Garrett, Wood and myself. Mr. Cary will not become a member until June 1, 1978, but he has attended both meetings of the POB held thus far. The fifth member has not yet been designated, but efforts are continuing to fill the position and we are hopeful of an early resolution.

The POB met for the first time on March 7, 1978 at which time general background and organizational matters were discussed. The second meeting was held on April 11, 1978 at which we discussed the role of the POB, the peer review program, proposed changes in the organization document relating to term, selection, removal and compensation of POB members and other matters, By-laws for the POB and employment of staff and other administrative matters. A further meeting of the POB has been called for May 17, 1978, and regular monthly meetings will probably be scheduled thereafter.

A representative of the POB, Mr. Richard Stark, my partner, has attended and reported to the POB on meetings of the Executive Committee of the SEC Practice Section on February 24, March 28 and April 17, and I have had meetings with executives and legal counsel for the Section regarding various matters.

The present members of the POB are scheduled to meet with you and other members of the Commission at 4 P.M. on May 17, 1978. The POB looks forward to this and future opportunities for an exchange of views with members of the Commission. On April 10, 1978 Mr. Stark met with Messrs. Ten Eyck and Golub on Clarence Sampson's staff and Mr. Stark or others representing the POB will have further meetings with SEC Staff members as needed. The POB plans from time to time to furnish information regarding its activities to you and your Staff.

As I indicated in my letter of April 4, the Executive Committee of the Section has recommended changes in the organization document of the Section to provide that after initial appointment of the POB, the POB shall, in consultation with and subject to the approval of the AICPA Board of Directors, appoint, remove and set terms and compensation of its members and select its chairman. A further amendment would make specific the obligation of the POB to publish an annual report. The POB was consulted in the preparation of these changes and approved them at the April 11 meeting. A copy of revised Section VII of the Division of Firms' organization document relating to the POB is annexed. Draft By-laws of the POB have been prepared and approved in principle and will be adopted after the organization document has been amended by action of the AICPA Board of Directors.

The POB has just hired Mr. Louis W. Matusiak as Executive Director to commence work on or about May 1, 1978. Mr. Matusiak is now a partner with Alexander Grant & Company in Chicago. The POB will probably be seeking at least one other person as an assistant to the Executive Director with respect to monitoring of the peer review program of the Section and other matters. Arrangements have also been made for office space for the POB staff in New York.

; The POB has reviewed its responsibilities and functions as set forth in Section VII of the organization document (annexed hereto). It is the initial conclusion of the POB that such description provides a practical and effective basis for action, consistent with the POB's view of its oversight role; and that the POB will have full authority to look into and comment on every aspect of the SEC Practice Section's

activities. While the POB does not have "line authority" and is not designed to be an appellate review board, it is the initial judgment of the POB that its power to monitor and review any and all matters and to make recommendations will enable it to act as an effective overseer of the self-regulatory effort being undertaken by the SEC Practice Section. The POB does not believe it would be necessary or desirable for its role to be expanded to one of direct responsibility for the SEC Practice Section's self-regulatory program. In the POB's view the self-regulatory scheme has been carefully considered and is being aggressively pursued. It should be given opportunity to function. The POB intends to maintain a continuing review of the self-regulatory program of the Section and will not hesitate to comment if in its view the program is not effective.

At the April 11 meeting the POB devoted its principal attention to the regular peer review program being developed by the Peer Review Committee of the Section. It is the impression of the POB that the regular peer review program represents a responsible approach to the objective of maintaining and applying quality control standards. Under the oversight concept, the POB does not have direct responsibility for conducting peer reviews or determining sanctions. However, the POB believes that the success of the peer review program is important and has concluded that certain aspects of the program should be monitored by its own staff. As noted above, plans are being made for the POB to employ necessary staff for this purpose.

There are a number of elements of the peer review program which remain to be considered by the POB. Among other matters, we will be reviewing the regular peer review program when it is in completed form, including standards for conducting and reporting on compliance reviews, we will be considering the question of whether regular peer reviews should be permitted on a firm-on-firm basis, and we will want to consider what peer review documents should be made available to the public.

The Planning Committee of the Executive Committee of the Section has asked the POB to make a recommendation regarding the scope of special peer reviews and sanctions undertaken as a result of particular audit failures. The issue is whether the Section should proceed promptly with disciplinary action even though

litigation is involved or threatened. In order to do this the special peer review would need to examine the specific case of the audit failure, which the organization document mentioned above does not now authorize. The POB recognizes that this question is exceedingly complex and that the rights and important interests of parties to litigation can be very seriously affected by the policy decision on this issue. This matter will be studied with utmost care and a hasty decision of the POB should not be expected.

At a later date the POB expects to address the question of the scope of management advisory services performed by CPA firms.

All members of the POB are cognizant of the heavy responsibilities which the POB must bear in the effective exercise of its oversight responsibilities and are committed to the diligent discharge of those responsibilities.

We look forward to seeing you on May 17.

Respectfully yours,



John J. McCloy