

United States Senate

WASHINGTON, DC 20510

January 25, 2023

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

Dear Chair Williams:

We write regarding recent turmoil in the cryptocurrency industry following the collapse of crypto platform FTX in November 2022,¹ and the role that auditors may have played in misleading the public about the financial soundness and safety of crypto companies. The ongoing reports of scandalous accounting practices in the crypto industry raise questions about crypto accounting firms' independence and the methods they employed to assess the integrity of crypto firms' financial statements,² underscoring the need for the Public Company Accounting Oversight Board (PCAOB) to act to ensure accountability. When PCAOB-registered auditors perform sham audits – even for firms that may lay outside of the PCAOB's jurisdiction – they tarnish the credibility of the PCAOB and undermine confidence in the PCAOB-registered auditors that investors and the public rely on when making investment decisions.

In July 2021, less than 16 months before filing for bankruptcy, former FTX CEO Sam Bankman-Fried touted that FTX had become “the first (?) crypto derivatives exchange to complete a [generally accepted accounting principles] GAAP audit.”³ In August 2021, Bankman-Fried announced that FTX's U.S. affiliate, FTX.US, had also “passed its US GAAP audit” and that both companies would “plan to continue getting audits going forward.”⁴ As questions about FTX's solvency began to swirl in November 2022, Bankman-Fried cited its “GAAP audits” in an effort to quell concerns and assure FTX customers of the safety of their assets.⁵ However, we now know that these audits, which were conducted by “Armanino, one of the 20 largest accounting firms in the country by revenue, and Prager Metis, which styles itself the first accounting practice to open a headquarters in the metaverse,”⁶ failed to identify the alleged “old-

¹ Reuters, “Exclusive: At least \$1 billion of client funds missing at failed crypto firm FTX,” Angus Berwick, November 13, 2022, <https://www.reuters.com/markets/currencies/exclusive-least-1-billion-client-funds-missing-failed-crypto-firm-ftx-sources-2022-11-12/>.

² Bloomberg Tax, “FTX Collapse Puts Auditors in Crosshairs of Clients, Regulators,” Nicola M. White, November 30, 2022, <https://news.bloombergtax.com/financial-accounting/ftx-collapse-puts-auditors-in-crosshairs-of-clients-regulators>.

³ Tweet by Sam Bankman-Fried, July 31, 2021, https://twitter.com/sbf_ftx/status/142135472191115776.

⁴ Tweet by Sam Bankman-Fried, August 26, 2021, https://twitter.com/sbf_ftx/status/1431087427154849795.

⁵ Cointelegraph, “SBF calls for collaboration with Binance ‘for the ecosystem,’” Ana Paula Pereira, November 7, 2022, <https://cointelegraph.com/news/sbf-calls-for-collaboration-with-binance-for-the-ecosystem>.

⁶ Financial Times, “FTX collapse puts its auditors in the spotlight,” Stephen Foley, November 13, 2022, <https://www.ft.com/content/930c6cea-5457-4dfa-9d47-666c0698c335>.

fashioned embezzlement,” “unprecedented” lack of recordkeeping, and “utter failure of corporate controls” at the heart of FTX’s collapse.⁷

In a November 2022 bankruptcy court submission, FTX’s new CEO, John J. Ray III, cited “substantial concerns as to the information presented in these audited financial statements” and said he did “not believe it appropriate for stakeholders or the court to rely on the audited financial statements.”⁸

While Armanino and Prager Metis have stood by their work, with Armanino claiming that “[it was] never engaged to audit internal controls” because FTX was not a publicly traded company,⁹ the accounting firms’ actions preceding FTX’s bankruptcy raise questions about whether they were acting as “crypto industry cheerleaders” – even though “auditors are required by regulators to maintain a ‘professional skepticism,’ including an alertness to significant errors and fraud, when assessing a company’s finances.”¹⁰ For example, Armanino openly praised a Securities and Exchange Commission (SEC) Commissioner when she “criticized the regulator’s plans to step up crypto enforcement.”¹¹ The audit firm also spotlighted its client, crypto exchange Kraken, when it encouraged regulators to move through the revolving door for higher pay.¹² Prager Metis similarly acted as a crypto cheerleader, writing on its website that it was “proud to support FTX US” and posting a photo on social media depicting its auditors attending a baseball game with FTX executives.¹³

Armanino and Prager Metis were not the only auditing firms cashing in on the crypto industry’s at best confusing and at worst deceptive attempts to convince investors of their safety and legitimacy. While the Big Four accounting firms – Deloitte, Ernst and Young, KPMG, and PricewaterhouseCoopers – have largely avoided providing formal auditing services to private crypto firms,¹⁴ Deloitte and PricewaterhouseCoopers reportedly advised FTX before its collapse.¹⁵ Other auditing firms, such as Mazars Group and Marcum, validated so-called “proof-

⁷ House Committee on Financial Services, “Investigating the Collapse of FTX, PT I,” December 13, 2022, <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=408483>; Written testimony of John J. Ray III to the U.S. House Committee on Financial Services, December 13, 2022, <https://docs.house.gov/meetings/BA/BA00/20221213/115246/HHRG-117-BA00-Wstate-RayJ-20221213.pdf>.

⁸ Bloomberg Tax, “FTX Collapse Puts Auditors in Crosshairs of Clients, Regulators,” Nicola M. White, November 30, 2022, <https://news.bloombergtax.com/financial-accounting/ftx-collapse-puts-auditors-in-crosshairs-of-clients-regulators>.

⁹ Insider, “FTX US’s auditor stands by its accounting work for the collapsed crypto exchange, report says,” Jennifer Sor, December 23, 2022, <https://markets.businessinsider.com/news/currencies/ftx-bankruptcy-sam-bankman-fried-fraud-auditor-armanino-fraud-2022-12>.

¹⁰ Wall Street Journal, “FTX Auditors Doubled as Crypto Industry Cheerleaders,” Jean Eaglesham and Patricia Kowsmann, November 17, 2022, <https://www.wsj.com/articles/ftx-auditors-doubled-as-crypto-industry-cheerleaders-11668709049>.

¹¹ *Id.*

¹² *Id.*

¹³ *Id.*

¹⁴ Bloomberg Tax, “Auditors Spurn Crypto After FTX, Misleading Reserve Estimates,” Amanda Iacone and Nicola M. White, January 3, 2023, <https://news.bloombergtax.com/financial-accounting/auditors-spurn-crypto-after-ftx-misleading-reserve-estimates>.

¹⁵ Forbes, “Stripe, Deloitte, Sullivan & Cromwell Are Among 53 FTX Advisors, Vendors And Bankers Weathering Exchange’s Collapse,” Javier Paz, Nina Bambysheva, and Emily Mason, November 10, 2022, <https://www.forbes.com/sites/javierpaz/2022/11/10/stripe-deloitte-sullivan--cromwell-are-among-53-ftx-advisors->

of-reserves” reports, which are intended to show that a crypto company providing custody services has assets that are equal to or greater than customer deposits.¹⁶

In reality, proof-of-reserves examinations fall significantly short of real audits, as proof-of-reserves reports do not follow established standards, are not overseen by the PCAOB, and do not prove that listed assets actually belong to customers.¹⁷ Yet some crypto companies have touted them as “audits” and evidence that they have the funds necessary to meet all depositor claims. Kraken, a major crypto exchange, claimed that it had been subjected to “‘next-generation audit standards’ that showed how the exchange was ‘exceeding the transparency offered by legacy financial firms.’”¹⁸ Crypto finance platform Yield App made similar claims, stating that it had “‘passed a ‘stringent’ reserves audit ‘with flying colors.’”¹⁹ Last month, the CEO of Binance, the world’s largest crypto exchange, touted its “[a]udited proof of reserves”²⁰ – even though Mazars’ report merely “‘consisted of a five-page letter” that “‘contained three numbers and didn’t express an opinion, meaning the auditor wasn’t vouching for the numbers.”²¹ Shortly after Mazars published Binance’s proof-of-reserves report, Mazars announced that it would suspend its work with Binance and other crypto firms, citing “‘concerns regarding the way these [proof-of-reserve] reports are understood by the public.”²² Armanino also announced that it would abandon its crypto industry work, citing “‘a pretty big gap in understanding between what an audit or a proof of reserve offering provides to the recipients of those reports.”²³

The PCAOB’s mission is to “‘regulat[e] the audits of public companies and SEC-registered brokers and dealers in order to protect investors and further the public interest in the preparation of informative, accurate, and independent audit reports.”²⁴ Following FTX’s collapse, you described the limits of the PCAOB’s jurisdiction, stating, “[t]he PCAOB only has jurisdiction over the audits of public companies and broker dealers. FTX was not a public company, and therefore the PCAOB could not inspect its audits.”²⁵ You also stated “‘that PCAOB-registered

[venders-and-bankers-weathering-exchanges-collapse/?sh=6bdc03d47f21](https://www.pcaob.org/about/mission-vision-values).

¹⁶ Bloomberg Tax, “Auditors Spurn Crypto After FTX, Misleading Reserve Estimates,” Amanda Iacone and Nicola M. White, January 3, 2023, <https://news.bloombergtax.com/financial-accounting/auditors-spurn-crypto-after-ftx-misleading-reserve-estimates>.

¹⁷ Wall Street Journal, “Here’s Why Crypto ‘Proof of Reserves’ Isn’t All It Appears to Be,” Paul Vigna, November 25, 2022, https://www.wsj.com/livecoverage/stock-market-news-today-11-25-2022/card/here-s-why-crypto-proof-of-reserves-isn-t-all-it-appears-to-be-cyHCapcHhzUxHNm4acAZ?mod=article_inline; The inability to prove customer ownership of assets is a crucial fault given what we witnessed in the FTX fallout: because crypto exchanges are not registered as brokers and therefore not required to separate customer deposits and company assets, the two can be comingled, jeopardizing customers’ ability to access their funds.

¹⁸ Bloomberg Tax, “Auditors Spurn Crypto After FTX, Misleading Reserve Estimates,” Amanda Iacone and Nicola M. White, January 3, 2023, <https://news.bloombergtax.com/financial-accounting/auditors-spurn-crypto-after-ftx-misleading-reserve-estimates>.

¹⁹ *Id.*

²⁰ Tweet by Changpeng Zhao, December 7, 2022, https://twitter.com/cz_binance/status/1600567141887000580.

²¹ Wall Street Journal, “Binance Says Accounting Firm Mazars Pauses Work for Crypto Clients,” Caitlin Ostroff and Jean Eaglesham, December 16, 2022, <https://www.wsj.com/articles/binance-says-accounting-firm-pauses-work-for-its-crypto-clients-11671200654>.

²² *Id.*

²³ Financial Times, “FTX US auditor Armanino defends work for failed crypto exchange,” Stephen Foley, December 23, 2022, <https://www.ft.com/content/42087255-92ad-45b7-b5ad-3b8457e0c1f8>.

²⁴ PCAOB, “Mission, Vision, and Values,” <https://pcaobus.org/about/mission-vision-values>.

firms” – such as Armanino and Prager Metis²⁶ – “only have to follow PCAOB standards and rules when they’re auditing a public issuer or broker dealer under our jurisdiction, not for any other clients.”²⁷ But this statement does not appear to be consistent with PCAOB Rule 3100, which states that “a registered public accounting firm and its associated persons shall comply with all applicable auditing and related professional practice standards,”²⁸ or PCAOB Rule 3200, which states that “in connection with the preparation or issuance of any audit report, a registered public accounting firm and its associated persons shall comply with all applicable auditing standards adopted by the Board.”²⁹ This rule is clearly not restricted solely to public companies.

Your efforts to ignore what is, at best, incompetence and inappropriate activity by large public auditors is not consistent with your “vision and values” statement that “The PCAOB will be a trusted leader that promotes quality auditing through forward-looking, responsive, and innovative oversight.”³⁰ If the auditors scrutinizing large public companies are the same auditors whitewashing “audit” results for crypto firms with demonstrated histories of malfeasance, investors and the public cannot have confidence in either set of audits. These misleading financial reports shake our confidence in the entire auditing industry. Moreover, some of these crypto firms arguably *should* fall within the PCAOB’s jurisdiction given the SEC’s position that companies performing broker-dealer functions in the crypto market should be registered as broker dealers.³¹ Regardless, the PCAOB must act to maintain its rigorous standards for audit firms.

While the SEC’s plans to ramp up oversight of crypto auditors is an important step,³² the PCAOB also has a responsibility to protect investors from shady and misleading auditing practices. Therefore, we request answers to the following questions no later than February 8, 2023:

1. What risks do retail investors face when crypto firms – whether publicly traded or private – attempt to pass off proof-of-reserve examinations as “audits” and what is the PCAOB doing to mitigate these risks?

²⁵ Thomson Reuters, “Chair Williams Says PCAOB Has No Authority to Inspect Audits of FTX,” Soyoung Ho, November 30, 2022, <https://tax.thomsonreuters.com/news/chair-williams-says-pcaob-has-no-authority-to-inspect-audits-of-ftx/>.

²⁶ PCAOB, “Registered Firms,” <https://pcaobus.org/oversight/registration/registered-firms>.

²⁷ Thomson Reuters, “Chair Williams Says PCAOB Has No Authority to Inspect Audits of FTX,” Soyoung Ho, November 30, 2022, <https://tax.thomsonreuters.com/news/chair-williams-says-pcaob-has-no-authority-to-inspect-audits-of-ftx/>.

²⁸ PCAOB, “Section 3. Auditing and Related Professional Practice and Standards,” https://pcaobus.org/about/rules-rulemaking/rules/section_3.

²⁹ *Id.*

³⁰ PCAOB, “Mission, Vision, and Values,” <https://pcaobus.org/about/mission-vision-values>.

³¹ Reuters, “Crypto intermediaries should register with U.S. SEC, agency chair says,” Michelle Price, September 8, 2022, [https://www.reuters.com/technology/crypto-intermediaries-should-register-with-us-sec-agency-chair-says-2022-09-08/#:~:text=WASHINGTON%2C%20Sept%208%20\(Reuters\),agency's%20chair%20said%20on%20Thursday](https://www.reuters.com/technology/crypto-intermediaries-should-register-with-us-sec-agency-chair-says-2022-09-08/#:~:text=WASHINGTON%2C%20Sept%208%20(Reuters),agency's%20chair%20said%20on%20Thursday).

³² Wall Street Journal, “SEC Heightening Scrutiny of Auditors’ Crypto Work,” Jean Eaglesham, December 22, 2022, <https://www.wsj.com/articles/sec-heightening-scrutiny-of-auditors-crypto-work-11671681693>.

2. Are PCAOB-registered auditors, or the private, non-broker dealer companies who receive their audit-like services, required to disclose to investors that those services are performed outside of the oversight of the PCAOB?
3. Was the PCAOB aware of potential conflicts of interest or other concerning behavior that betrayed a lack of professional skepticism by Armanino or Prager Metis and their client FTX before FTX's collapse?
 - a. If so, did the PCAOB provide any warnings to Armanino or Prager Metis about this behavior? Please provide copies of any communications between PCAOB and the accounting firms.
4. Does the PCAOB restrict PCAOB-registered auditors from publicly praising or endorsing the companies they provide services to? Please provide relevant guidance governing public endorsements or praise of clients.
5. Does the PCAOB have the authority to strip auditors of their PCAOB-registered status if they provide services or engage in conduct that fall short of PCAOB standards and rules, even if those actions are taken in relation to private, non-SEC registered companies?
6. PCAOB Rule 3100 states that "A registered public accounting firm and its associated persons shall comply with all applicable auditing and related professional practice standards."³³ Were the activities of Armanino and Prager Mentis on behalf of FTX, and of Mazars on behalf of Binance, consistent "with all applicable auditing and related professional practice standards"?
 - a. Please explain how PCAOB assesses compliance with Rule 3100 and describe any instances of actions taken against firms found to be out of compliance.
7. PCAOB Rule 3200 states that "in connection with the preparation or issuance of any audit report, a registered public accounting firm and its associated persons shall comply with all applicable auditing standards adopted by the Board."³⁴ Were the activities of Armanino and Prager Mentis on behalf of FTX, and of Mazars on behalf of Binance, consistent with this standard?
 - a. Please explain how PCAOB assesses compliance with Rule 3200 and describe any instances of actions taken against firms found to be out of compliance.
8. In May 2022, the PCAOB released a public version of a 2020 inspection report for Prager Metis in which it found deficiencies in all four audits the agency reviewed, including a failure to "evaluate revenue projections developed by the issuer" and a failure to "identify, and appropriately address, the issuer's omission of certain disclosures."³⁵ Since its inspection, what steps has the PCAOB taken to ensure that Prager Metis has corrected these deficiencies?

³³ PCAOB, "Section 3. Auditing and Related Professional Practice and Standards," https://pcaobus.org/about/rules-rulemaking/rules/section_3.

³⁴ *Id.*

³⁵ PCAOB, "2020 Inspection, Prager Metis CPAs LLP," May 13, 2022, https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/inspections/reports/documents/104-2022-137-pragermetis-ca.pdf?sfvrsn=63752e71_4.

- a. The May 2022 inspection report notes that “Portions of the complete report are omitted from this document in order to comply with Sections 104(g)(2) and 105(b)(5) (A) of the Sarbanes-Oxley Act of 2002” and that per Section 104(g)(2) of Sarbanes-Oxley, “If a firm does not address to the Board’s satisfaction any criticism of, or potential defect in, the firm’s system of quality control within 12 months after the issuance of our report, we will make public any such deficiency.”³⁶ Does the PCAOB intend to publicly release the remaining portions of Prager Metis’ inspection report in May 2023?
9. In June 2019, the PCAOB released a public version of a 2018 inspection report for Armanino in which it found multiple deficiencies, including one “of such significance that it appeared to the inspection team that [Armanino], at the time it issued its audit report, had not obtained sufficient appropriate audit evidence to support its opinion that the financial statements were presented fairly, in all material respects, in conformity with the applicable financial reporting framework. In other words, in this audit, the auditor issued an opinion without satisfying its fundamental obligation to obtain reasonable assurance about whether the financial statements were free of material misstatement.”³⁷ Since its inspection, what steps has the PCAOB taken to ensure that Armanino has corrected these deficiencies?
 - a. Has the PCAOB publicly released the remaining portions of the 2018 inspection report? If not, why?
 10. Will you commit to using your inspection authority to evaluate and publicly report on auditors that provided services for any crypto company acting as a broker dealer, even if the firm was not registered as such with the SEC?
 11. While the Big Four accounting firms have largely avoided providing auditing services to the risk-laden crypto industry, their subsidiaries “have at least a dozen [crypto-affiliated] audit clients listed on public stock exchanges globally including Coinbase Global Inc., WisdomTree Inc., Northern Data AG, and Bitfarms LTD/Canada—companies that meet strict audit, disclosure, and other regulatory requirements that come with a public listing.”³⁸ Please describe the standards established by the PCAOB for these audits and the PCAOB’s assessments of the audits for these crypto-affiliated clients.
 12. Banks, publicly traded companies, and registered investment funds maintain large investments in crypto firms, including FTX, and in some cases may hold digital assets on their balance sheets.³⁹ Given that audits of these companies would unquestionably fall within

³⁶ *Id.*

³⁷ PCAOB, “Report on 2018 Inspection of Armanino LLP,” June 20, 2019, https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/inspections/reports/documents/104-2019-105-armanino-llp.pdf?sfvrsn=af93a642_1.

³⁸ Bloomberg Tax, “Auditors Spurn Crypto After FTX, Misleading Reserve Estimates,” Amanda Iacone and Nicola M. White, January 3, 2023, <https://news.bloombergtax.com/financial-accounting/auditors-spurn-crypto-after-ftx-misleading-reserve-estimates>.

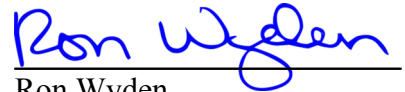
³⁹ New York Times, “Investors Who Put \$2 Billion Into FTX Face Scrutiny, Too,” Erin Griffith and David Yaffe-Bellany, November 11, 2022, <https://www.nytimes.com/2022/11/11/technology/ftx-investors-venture-capital.html>; CoinDesk, “Goldman Sachs to Spend ‘Tens of Millions’ on Discounted Crypto Investments After FTX Implosion: Report,” Eliza Gritsi, December 6, 2022, <https://www.coindesk.com/business/2022/12/06/goldman-sachs-to-spend-tens-of-millions-on-discounted-crypto-investments-after-ftx-implosion-report/>; CoinGecko, Bitcoin Holdings by

the jurisdiction of the PCAOB, please describe the standards by which auditors must abide when evaluating the risk of exposure to crypto firms or validating the valuation of crypto investments.

Sincerely,



Elizabeth Warren
United States Senator



Ron Wyden
United States Senator

Public Companies, <https://www.coingecko.com/en/public-companies-bitcoin>; MarketWatch, “FTX problems mean big headaches for its private equity investors,” Steve Gelsi, November 9, 2022, <https://www.marketwatch.com/story/ftx-problems-mean-big-headaches-for-its-private-equity-investors-11668015499>.