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June 14, 1978

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

Dear Mr. Chairman:

I have your letter of June 2nd and I have distributed copies of it to the members of the Public Oversight Board and copies have been made available to the Executive Committee of the SEC Practice Section of the AICPA. Our Board appreciates the thoughtful comments and suggestions in your letter and the interest which we share in the effective self-regulatory program of the accounting profession. Simultaneously with the receipt of your letter the members of the Board met with members of the Planning Committee of the Executive Committee of the Section on the afternoon of June 5th and discussed, among other things, the contents of your letter. I understand that a meeting of the Executive Committee of the Section was held on June 6th at which your letter was discussed and consideration was given to suggestions which have been made to ensure that the work of the peer review program proceeds not only efficiently but with due regard to the credibility of its work as an important element in the self-regulatory program of the profession. Taking up in order the subject paragraphs of your letter I think it appropriate to comment now briefly on those paragraphs.

Structure and Administration of the SEC Practice Section.

The members of the Public Oversight Board, while they are quite clear in their determination not to assume line responsibility for the self-regulatory program of the Institute, do intend to monitor the program so as to be in

a position to express their views quite independently as to the effectiveness of the self-regulatory process and to make from time to time reports and recommendations, which will, under appropriate circumstances, be made public. To this end, as you note in your letter, a number of changes in the organization document have already been made, some at our suggestion, which should effect a viable and independent structure on which the self-regulatory system is based.

The Board realizes the importance of its members' independence and commitment. However, if the Section's program is to be self-regulatory, in the last analysis the record of its activities will determine both its effectiveness and its credibility. The Board will be in a position to evaluate the effectiveness of the Section's work. In my judgment it is the record which will earn acceptance and recognition rather than the forms which are initially devised to accomplish the results.

Peer Review Program

The Board has had a number of meetings at which we have discussed the format of the peer review program and, with the assistance of my partner, Mr. Stark, I have kept in close touch with the discussions which have taken place between representatives of the AICPA and your own staff. I do not gain the impression from my talks with representatives of the AICPA that the program stands perilously close, as you put it, to a self-serving effort conducted behind closed doors. I believe they are trying sincerely, and I hope with our Board's guidance, they will be able, to develop a peer review program which will be efficient and at the same time provide independence and objectivity.

The Board has encountered no resistance from the AICPA representatives to the power or the authority of the Board to observe the peer review process in the field and to review its programs. It will take some time before we know just how much in the way of staff the Board will require in order to carry out its monitoring program in this regard, but I feel that whatever in reason it requires will be afforded.

On the matter of access to the documents, we have encountered no obstacle to the Board's right of access, but I do sense that there are definite problems in granting to the Commission broad access to documents developed

as part of the review process. This topic will require further discussion.

We are also conscious of the need to give further attention to the question of publicity in regard to the reviews and I am hopeful that a satisfactory resolution of this problem will be forthcoming. We are also seeking a resolution on the problem of possible limitations on the scope of the peer reviews, particularly in cases where litigation may be threatened or pending. This is a troublesome problem, but it is hoped that the Board and the AICPA will be able to establish a satisfactory modus operandi.

The Board recognizes the need to satisfy itself as to the quality of engagements performed outside the United States and it recognizes that this is an area in which its views may properly be sought.

Management Advisory Services.

Although the question of the proper scope of management advisory services is a difficult one, the Board is convinced that it is a matter which the Board should address itself to without undue delay. I have asked that Messrs. Garrett and Wood look into this question and on their recommendation the Board has under consideration holding public hearings on this subject probably during this Summer. There is need to learn the scope of the problem, the extent to which both large and small firms are engaged in these services, and the possible effects the rendering of these services may have on independence. The Board is reviewing the substantial existing public record on this subject to determine whether public hearings will add enough to our understanding of the issues to be worthwhile.

Although there are some difficult problems and some imponderable ones that I see ahead, I can assure you that the members of the Board are determined to apply their best judgment to them to the end that the Board's oversight of the self-regulatory process will prove to be a meaningful and effective element in the whole self-regulatory process.

I am conscious, as are my colleagues on the Board, of the reliance that the SEC places on the Board as an important link to the effective self-regulation of the profession. As I have said, we intend to apply ourselves

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within our competence fully to our responsibilities, but I would point out that the chief element in the success of a self-regulatory program will lie in the integrity and effectiveness with which the profession itself carries it out. I feel that AICPA has evidenced the seriousness of its purpose in setting up the self-regulatory structure and, particularly, in that it has been willing to give the authority it has to the Public Oversight Board composed wholly of non-members of the profession, as a further means of achieving and maintaining this integrity and effectiveness.

Sincerely,

A handwritten signature in cursive script, appearing to read "John J. McCloy".

John J. McCloy, Chairman
Public Oversight Board