

STATEMENT OF KAYLA J. GILLAN

December 14, 2004

***Proposed Ethics and Independence Rules
Concerning Independence, Tax Services, and Contingency Fees***

Thank you, Mr. Chair, Mr. Carmichael, and Ms. Rivshin.

I am very pleased to support the proposal before us today, and look forward to what I trust will be a thorough and constructive public comment period. I would like to emphasize a couple of points, and to ask a couple of questions.

First, I would like to share the evolution of my own thought processes, in the hope that it may be helpful to others as they consider this proposal. As some of you may know, during the SEC's regulatory efforts in 2000 – and again during the Congressional debate immediately prior to the passage of the Sarbanes-Oxley Act of 2002 – I argued that auditors should be prohibited from performing any and all non-audit services to their audit clients. The reason was simple: any effort to permit some but prohibit other non-audit services would, I feared, encourage definitional game-playing and further erode investor confidence in auditor integrity. I also acknowledge that when this Board first began to gather information on this issue, my initial instincts remained somewhat cynical. I have, however, been informed and influenced by several intervening events:

- ◆ As a result of our roundtable on the impact of tax services on independence (held last July), I learned that the auditor's involvement in a company's decisions about the appropriate tax treatment of some transactions can actually play a significant role in assuring the accuracy not only of annual financial statements but quarterly disclosures as well.
- ◆ I also learned more about the wide range of tax services that have historically been included under the broad description of "tax compliance, advice and planning," and about the impact that each type of service can have on the auditor-client relationship. The hearing in October of 2003 by the Senate Finance Committee, and last June by the Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises, of the House Committee on Financial Services, have been particularly instructive in this regard.

- ◆ I am impressed with the data demonstrating how seriously and conscientiously audit committees are taking their responsibility to pre-approve all non-audit services proposed for their independent auditor.
- ◆ I have been reassured and comforted by the extraordinary impact that the PCAOB can play through its vigorous inspection program. We now have the tools (tools that didn't exist before Sarbanes-Oxley) to ensure that definitional games cannot be used to avoid the ethical standards that this Board adopts.

Throughout this process, I have tried to maintain focus on what I consider to be our two fundamental objectives. First, independence is not just a question of fact (does an auditor, in fact, have the requisite level of objectivity to make the hard judgments necessary to ensure accurate reporting to investors?). It is also a question of perception (will investors question the auditor's objectivity, under a given set of circumstances?). Second, we should not let the very important independence "tree" make us lose sight of the "forest" – which is high quality audits. That is, it is important to have both a high quality audit and the perception of one; it is not acceptable to only have the perception.

With the benefit of these many moving parts, I am very pleased with the proposal and, again, look forward to healthy debate. As a life-long consumer advocate (whether the product being consumed is baby food or professional services), I am particularly hopeful that this proposal will further assist audit committees in the very tough purchasing decisions that they face in today's climate.

I would also like to thank Doug Carmichael, Bella Rivshin and Greg Scates for their work on this proposal. You've spent many long hours, and the quality of your efforts continues to set a high bar for this Board to try to meet. I also thank Samantha Ross, Gordon Seymour and Kathleen Peters, for your insights and experiences. At the risk of being redundant, I am so proud of the wonderful example of teamwork that all of you, individually and collectively, continuously model for us.

Turning to my question: we've talked about what the proposal would prohibit and why. I'd like you to discuss in more depth the types of tax services that the proposal would not prohibit (specifically, compliance, ex-pat services, and routine tax planning and advice), and particularly why, at this time, you believe that these services should not (and should not be perceived as) impairing objectivity.