

**Written Testimony of Kayla J. Gillan<sup>1</sup>**

**Former Founding Member of the  
Public Company Accounting Oversight Board**

**Meeting of the Advisory Committee on the Auditing Profession**

**June 3, 2008**

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It is a pleasure to be with you today. Before I begin, I must ensure that the record is clear: I am speaking to you today as a former and founding member of the PCAOB, and as long-time investor advocate. I am not speaking on behalf of my current employer, RiskMetrics Group. The views I express are my own, and are not necessarily those of RiskMetrics, its subsidiary ISS, its board or staff.

Thank you for your kind invitation to offer my comments on your draft report. Let me say, first, that this is an extraordinarily thoughtful report, highlighting the critical issues that face the auditing profession. I commend you for the thoroughness of your analysis.

Your draft report contains five primary recommendations concerning the human capital issues impacting the auditing profession. Each is critical. However, in my view, the first recommendation – concerning implementing market-driven, dynamic curricula that help prepare new graduates to perform high quality audits – is the most important. The fact that our accounting and auditing curricula is so lagging the real world is the cause of many of the other problems identified throughout your report. It's like the children's game of mousetrap, where a ball transcends through a rickety device, triggering other calamitous events as it makes its way through the course. For example, if our colleges and universities were better able to prepare accounting students to "hit the ground running" upon graduation, then accounting firms would be able to decrease their considerable commitment to providing basic auditing education to new graduates. The firms would then be able to provide more resources to funding the development of faculty and faculty research, as suggested in your third recommendation.

I also applaud your second recommendation, concerning increasing the representation of minorities in the auditing profession. However, when reading the report I was startled by the absence of any discussion of the representation

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<sup>1</sup> Kayla J. Gillan served on the Public Company Accounting Oversight Board (PCAOB) from January 2003 – January 2008. Previously, Ms. Gillan was General Counsel for the California Public Employees' Retirement System (CalPERS). Ms. Gillan serves as chief administrative officer for RiskMetrics Group, Inc.

of women, and in particular of the wage disparity that continues to exist between the genders within the profession. According to the U.S. Census Bureau (and based on 1999 data), women between the ages of 35 and 54 with a Bachelor's degree or higher who work as accountants or auditors represent 42.6% of the profession, but earn only 72.9 cents of every dollar earned by their male counterparts.<sup>2</sup> According to a recent study conducted with the support of the AICPA's Work/Life and Women's Initiatives Executive Committee, women make up 19% of all public accounting firms' partners; while this is up from 12% a decade ago, the pace of advancement – 7 percentage points in 10 years – is disheartening.<sup>3</sup> We cannot expect women to join a profession in which their earning capacity is so disparate. I urge you to consider this issue as you finalize your report.

As I mentioned, your third recommendation concerns increasing the supply of qualified accounting faculty through, among other avenues, increased public and private funding of academia and research. As you are no doubt aware, the Sarbanes-Oxley Act includes an interesting provision, through which monetary penalties assessed by the PCAOB against registered firms and persons are to be used exclusively to fund merit-based scholarships for accounting undergraduate and graduate students.<sup>4</sup> This provision also includes, however, certain procedural requirements (including approval by Congress through an appropriations act) that, I believe, make implementation both difficult and inconsistent with the need to put these funds quickly to work. As we speak, a civil penalty of \$1 million, collected by the PCAOB last December, sits ready to contribute toward this important cause.<sup>5</sup> I suggest that, if you have not already done so, this Committee consider recommending eliminating the unnecessary procedural obstacles contained in the statute.

I would be remiss if I did not also comment on a suggestion by the task force established by the American Accounting Association (AAA) to monitor the activities of this Committee. Specifically, in its comment letter dated May 15, 2008, the task force suggested this Committee encourage the PCAOB to grant academics access to confidential inspection data for the purpose of conducting

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<sup>2</sup> Evidence From Census 2000 About Earnings by Detailed Occupation for Men and Women (U.S. Census Bureau, May 2004), p. 16.

<sup>3</sup> See <http://www.webcpa.com> (June 29, 2006).

<sup>4</sup> See Sarbanes-Oxley Act of 2002, Section 109(c)(2).

<sup>5</sup> See [http://www.pcaobus.org/Enforcement/Disciplinary\\_Proceedings/2007/12-10\\_Deloitte.pdf](http://www.pcaobus.org/Enforcement/Disciplinary_Proceedings/2007/12-10_Deloitte.pdf).

audit-practice research. I have long advocated greater transparency of information derived from the PCAOB inspection process. This being said, I am concerned with providing greater access to this information only to academics. If the Committee believes – as do I – that more transparency of PCAOB inspection data and findings would help promote higher quality audits, then I would urge you to recommend appropriate legislative amendments that would provide this information to all (and in particular to consumers of audit services), not just academics.

Before closing, Chairman Levitt asked me to comment on an issue not contained in your draft report, but upon which I know that you have spent considerable time in debate. Should audit firms be protected from catastrophic liability through caps or some other device? If so, should this protection be in exchange for greater transparency about firm financial structures and resources?

This is an issue that has been discussed and debated for decades. Quite frankly, I have seen nothing – during my time on the PCAOB, before or after – that has convinced me that caps on auditor liability are either necessary to protect the sustainability of the auditing profession, or wise public policy. In my view, the best protection auditors have against catastrophic liability is to faithfully follow the professional standards that are in place. I know of no instance in which an auditor or audit firm has been found liable for damages sustained by investors when they have followed professional rules and standards.

Please understand: I am not a defender of our current securities litigation system. I think it contributes to an obscene waste of this country's capital, and there is much that I would change about it. But I do not believe that one class of potential defendants – even a class as important to the functioning of our securities markets as are auditors – should be protected at the expense of all other parties. I see this type of patchwork protectionism as akin to pushing a ball of Jell-o uphill. As you seek to protect one type of defendant through pushing the Jell-o in one spot, it simply squirts out in another. If auditors – who already under federal law are responsible only for their proportionate fault – have their liability more greatly limited, whose obligations will increase? Will public companies or other third parties have to pay the balance of legitimate damages? Or will wronged investors end up holding the bag? I urge the Committee not to ignore the impact on the larger litigation system, and to other parties, that would result from a liability cap for auditors. At most, this issue should be referred to a body with a larger public policy mandate – one that is looking at our litigation system from a holistic perspective.

Thank you again for your invitation to speak. Congratulations on your work to date, and I wish you much success as you complete this important assignment.