

**Prepared Statement of
Eric J. Keller, Chief Operating Officer, Kleiner Perkins Caufield & Byers
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Chairman Doty, Commissioners and Staff of the PCAOB:

Thank you for providing me the opportunity to participate in today's public meeting to discuss proposals to enhance auditor independence, objectivity and professional skepticism, including the potential for rules regarding auditor rotation.

My own perspective is based on 30 years as a finance executive here in Silicon Valley for both private and public companies and, more recently, as the chief operating officer for a venture capital firm. I am interested in the auditor rotation proposal both in how it would affect the more than 200 portfolio companies that we are investors in and the annual audits for our venture funds.

All of us whose careers involve financial reporting strongly agree with the importance of having independent, objective auditors who approach the financial statements of clients with relevant industry expertise, full understanding of accounting principles and a healthy dose of professional skepticism. The key question is whether mandatory auditor rotation is the best approach for improving the accountability of auditors. I agree that there are challenges with the current system, including conflicts for auditors who, once having issued reports on financial statements, subsequently conclude that those statements are wrong. However, I don't think that 'term limits' for auditors are the best approach to addressing these challenges. Here, briefly, are my reasons:

First, I believe that boards of directors are best positioned to make auditor decisions and should retain responsibility for appointing – and, if appropriate, changing – auditors. Today, finance executives, audit committees and auditors operate under tremendous pressure to get financial statements and associated disclosures 'right.' This pressure reflects a strong sense of fiduciary responsibility to investors, liability concerns under securities regulations and, importantly, inspections performed by the SEC and PCAOB. Candidly, the strongest possible warning to auditors against getting coopted by their clients took place with the dismantling of Arthur Andersen.

Second, term limits for auditors are as likely to weaken audits and financial reporting as to strengthen them. For example, rather than “cleaning up its act” just prior to a new auditor coming on board, the existing audit firm is more likely to aggressively defend its accounting subsequent to the auditor change. In addition, audit firms may have reduced incentives to staff ‘end of term’ audits with the best resources. This is a concern due to the complexity of accounting rules that place a heavy burden on auditors to fully understand client systems, processes and controls as well as GAAP and regulatory financial reporting requirements.

Third, the number of audit firms capable of conducting audits for many organizations is very limited and may be further narrowed by conflicts. Audit firms differ considerably in the depth of their expertise by geographic area, industry, and stage of company. Finding an audit firm that understands your industry is critical and mandatory rotations could reduce incentives for firms to develop deep domain expertise, particularly in rapidly emerging industries.

Finally, changing auditors will involve considerable direct and indirect costs as the new auditor gets up to speed. For large, global organizations, it may require much more than a single annual audit cycle before the new audit firm adequately understands the client organization. Inevitably, there will be a significant productivity loss for both auditor and client.

In the absence of evidence clearly linking restatements and audit failures to lack of auditor objectivity and skepticism, I suspect that the most important causes of these failures are the burgeoning complexity of financial reporting, greatly expanded disclosures and the increased precision required for financial statements. As an example, venture capital firms determine fair value for their investments in private companies pursuant to ASC 820. In some cases we use a differential equation created by two famous financial theorists to establish the value of an early stage company that is years away from revenue. Discussions with auditors on the application of valuation models, input assumptions, and sensitivity analyses involve substantial time and costs. In my view, the results suffer from a problem of implied precision – the option pricing model generates a very specific answer. However, whether this output is useful to investors in assessing the value of the early stage company is another matter.

So, what more can be done to enhance auditor independence, objectivity and professional skepticism? In the absence of magic bullets, I think we need to focus on basics:

- First, leverage audit committees to hold auditors and finance teams to high standards and ensure that auditors both appear and are independent. This means setting expectations for performance of both management and auditors; having robust discussions about financial reporting matters and audits; and challenging management to reconsider historical accounting policies as a business evolves.
- Second, continue rotations of lead audit partners and require detailed disclosure on non-audit related services performed by audit firms.
- Third, continue audit firm inspections by the PCAOB that are having a very significant impact.
- And finally, publicize the causes of audit failures so that audit firms, public companies and audit committees understand the issues and take seriously their responsibility to address them.

These steps may not sound as powerful as mandatory rotation but, in the long term, I think they will have a bigger impact. Once again, thank you for inviting me to participate in today's discussion.