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Where Have the Auditors Gone Wrong? An Analysis of SEC Accounting and Auditing Enforcement Releases

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The accounting scandals that have been publicized in recent years have prompted the question as to why auditors have failed to detect such misstatements. Accordingly, auditors have recently been the focus of much attention. As a result, changes (e.g., the Sarbanes-Oxley Act) have been implemented to help improve the financial reporting process. The purpose of this study was to determine the nature of audit deficiencies, as well as changes, if any, over time by a review of Accounting and Auditing Enforcement Releases issued by the Securities and Exchange Commission from 1997 - 2004. Overall, the nature of the most prevalent audit deficiencies relate primarily to the failure to exercise appropriate judgment. In numerous instances, auditors did not exercise due professional care and did not obtain sufficient and competent evidence – largely as a result of over-relying on their clients' representations. Perhaps knowing the specific audit issues surrounding recent alleged audit failures can help auditors avoid repeating the same mistakes and can ultimately help strengthen the integrity of the financial reporting process.

The accounting scandals that have been publicized in recent years have prompted the question as to why the auditors failed to detect such misstatements. In a speech to the International Financial Law Review on March 25, 2003, Paul S. Atkins, SEC Commissioner, stated that "because these corporate failures stemmed from lax accounting and corporate governance practices, 'Corporate Responsibility' became an important political issue in the United States, for the first time in perhaps 70 years." Numerous questions have been raised about the integrity of the financial reporting process and the overall effectiveness of the audit process. As a result, significant changes are underway, many of which stem from the Sarbanes-Oxley Act enacted in July 2002.

A helpful start to improving the audit process is to understand the areas in which auditors have made mistakes in the past. Accordingly, as a result of section 704 of the Sarbanes-Oxley Act of 2002, the SEC reviewed all enforcement actions involving violations of report-