**WHERE ARE THE ACCOUNTING PROFESSION’S LEADERS?**

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***Grumpy Old Accountants, May 8, 2011***

Recently, the Investor Advisory Group (IAG) of the Public Company Accounting Oversight Board (PCAOB) noted two diametrically opposed viewpoints that prompted us to wonder where the accounting profession’s leadership has gone. Not surprisingly, almost three years after the largest global financial crisis, the IAG confirmed what most of us have known:

*The recent financial crisis presented auditors, and by extension the Sarbanes-Oxley Act audit reforms, with their first big test since these reforms were put into place.* ***By any objective measure, they failed that test*** *(emphasis added).*

What is unbelievable, however, is a quote attributed by the IAG to the profession’s newest lobbyist group, the Center for Audit Quality (the CAQ):

*We believe that auditors generally carried out their role effectively during the crisis and appropriately reached audit opinions within the context of the applicable accounting and auditing frameworks.*

In other words, the CAQ, whose “leadership” is comprised of the CEOs of the largest U.S. accounting firms as well as the chairman of the American Institute of CPAs, intimates that the accounting profession bears little or no responsibility for the financial crisis of 2008. As if this were not damning enough, the UK auditors of the Big Four accounting firms recently argued before the House of Lords Economic Affairs Committee, that their audits of major banks were legally sound and that they were not in a position to raise alarm in markets about their banking clients’ business models. If the auditor is not in such a position, then who is? A parliamentary report described this defense as "disconcertingly complacent."

Arthur Andersen (the man), Leonard Spacek, and Eli Mason must be turning in their graves as they witness their beloved profession hopelessly adrift and approaching a precipitous fall. Do we believe that these icons, who provided the profession with a moral compass for nearly half century, would attempt to avoid responsibility using the “we complied with GAAP and GAAS” defense? The profession’s leadership crisis is so severe that calls for audit change come from most all quarters, except accounting academia of course, where professorial self-interest is aligned with that of the large accounting firms who fund teaching and research grants and hire students.

Stephen Haddrill, Chief Executive of the UK Financial Reporting Council, in a recent speech indicated that:

*The gap between what audit does and what users expect from an audit of the financial statements has been growing for the last 20-30 years, despite previous attempts to bridge it. Now is the time for fresh thinking to address that expectations gap and to bring the value of audit closer to investor needs in the modern economy.*

And the PCAOB agrees. According to its Chief Auditor and Director of Professional Standards, Martin F. Baumann:

*The auditor's reporting model is a top standard-setting priority of the Board. To better inform their investment decisions, investors say they need to hear more from the auditor about the risks the auditors faced in the audit and about the judgments and estimates management used in the financial statements.*

However, what’s the likelihood that meaningful, effective change in auditing will occur? David Callahan, author of the *Cheating Culture*, questions whether the accounting profession can ever reform itself. After all, auditors have a history of repeating their mistakes which began with stock market collapse in 1929, progressed to corporate frauds of the 1960s and early 1970s, continued through the savings and loan scandals of the 1980s, devolved into Enron and WorldCom, and culminated with the recent banking crisis. And we easily can predict that without substantive changes, auditors will continue to make mistakes that lead to tragic consequences for the market place.

Meaningful change requires leadership that the profession is sorely lacking. Big Four partners would rather spend time managing their litigation, than addressing the reasons the litigation arose: a flawed audit model. Francine McKenna estimates that the “leadership” in Big Four firms spends up to 75 percent of their time on litigation matters and as much as 15 percent of their firm revenues on litigation protection. And now these same firms are fighting Dodd Frank over worries that their flawed audit work will subject them to increased global lawsuits. Imagine if such resources were devoted to developing an audit model that worked. The investing public might actually benefit and the number of lawsuits might actually decline.

KPMG’s recently discovered internal control reporting blunder at Citicorp highlights the urgency of the audit model issue. KPMG issued a “clean” internal control report on Citicorp on February 22, 2008, despite the engagement partner’s knowledge on February 14, 2008 of material weaknesses found by bank examiners. Apparently, Big Four firms evaluate internal controls about as well as they can audit financial statements.

Tom Selling has gone so far as to suggest that part of the audit model problem might be that:

*…auditors might be good at verification of things which are capable of being verified, and very little else.*

If Tom is right, then we may be closer to the edge of the fall than we realized, and too late for even credible leadership to help.

*This essay reflects the opinion of the authors and not necessarily the opinions of The Pennsylvania State University, The American College, or Villanova University.*