

Austin Mitchell

Prem Sikka

**DIRTY BUSINESS: THE UNCHECKED
POWER OF MAJOR ACCOUNTANCY
FIRMS**

Association for Accountancy & Business Affairs

*Shedding light on darker practices
Working for an Open and Democratic Society*

The **Association for Accountancy & Business Affairs** (AABA) is an independent and non-profit making body limited by guarantee (company number 3480632). AABA is funded entirely from donations and subscriptions from individuals concerned to make the world a better place. AABA is devoted to broadening public choices by facilitating critical scrutiny of accountancy and business affairs. AABA will publish monographs and papers to advance alternative analysis and public policy reforms. Its principal objects are:

- (i) to advance the public interest by facilitating critical scrutiny of commercial and non-commercial organisations *inter alia* companies, partnerships, sole traders, public bodies, local authorities, charities, non-profit making organisations and any other form of commercial or non-commercial organisation;
- (ii) to facilitate critical scrutiny of professional bodies, regulatory bodies, employer organisations, employee organisations, government departments and business organisations;
- (iii) to campaign for such reforms as will help to secure greater openness and democracy, protect and further the rights of stakeholders and to make disclosures where necessary;
- (iv) to engage in education and research to further public awareness of the workings, the social, political and the economic role of accountancy and business organisations.

Please support AABA to achieve its aims. All donations and inquiries should be addressed to the **Association for Accountancy & Business Affairs**, P.O. Box 5874, Basildon, Essex SS16 5FR, UK.

DIRTY BUSINESS: THE UNCHECKED POWER OF MAJOR ACCOUNTANCY FIRMS

**Austin Mitchell
House of Commons
Member for Great Grimsby, UK**

**Prem Sikka
University of Essex, UK**

ISBN 1-902384-07-5

**First published in 2002
Association for Accountancy & Business Affairs
P.O. Box 5874, Basildon, Essex SS16 5FR, UK.**

**© Association for Accountancy & Business Affairs
All rights reserved.**

No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means, electronic, mechanical, photocopying or otherwise, without the prior written consent of the publishers.

<http://visar.csustan.edu/aaba/aaba.htm>

AUDITORS WANTED

Major British companies require technically qualified auditors. The work is unsuitable for those with a social conscience.

The job is extremely well paid and secure. The market for auditing is guaranteed by the state. You can audit the same company for years and there is no independent measure of your performance. The right candidate can earn bonuses and promotion by using audit as a market stall to sell other services. Specialists in tax avoidance/evasion are especially welcome. Training to launder money is available. Special bonuses for innovative ways of massaging company accounts, forming offshore companies, devising off-balance sheet financing schemes and lightening tax burdens for the rich.

Successful candidates should be ready to devise and use irregular practices and falsify audit work. The ability to shred key documents at short notice is an advantage. Our experienced staff will provide expert training. You will not owe a 'duty of care' to any individual stakeholder. You will not be required to publish any information about your affairs. Your activities are lightly regulated by soft touch regulators who are sympathetic to auditors and their firms.

The standards of auditing are not demanding. Interest free loans, housing and favours from audit clients can be freely accepted. Fully bonded protection is available as our Institute is vastly experienced in whitewash and cover-up. You will learn how to individualise audit failures and blame everyone else for your shortcomings. No international regulator will gain access to your working papers. The Department of Trade and Industry will provide lucrative consultancy contracts but negligent audit firms will not be prosecuted. Political parties, politicians and ministers have been trained to understand your needs.

Please do not apply if you have concerns about audit failures causing loss of pensions, jobs, investments, savings and taxes must not apply. **Send your CV and a list of achievements to any major accountancy firm and the Institute of Chartered Accountants. Copies should also be sent to the Secretary of State for Trade & Industry, Department of Trade & Industry, 1 Victoria Street, London SW1H 0ET.**

DIRTY BUSINESS: THE UNCHECKED POWER OF MAJOR ACCOUNTANCY FIRMS

CONTENTS

Executive Summary	2	
Danger: Accountancy Firms at Work	3	
The Seeds of Audit Failures		8
Money, Money, Money	11	
Silence Please: Auditors at Work	23	
Structural and Cultural Problems	29	
Global Unaccountability	38	
Shielding the Auditing Industry	44	
Summary, Discussion and Proposals for Reform	50	
Appendix 1	59	
Bibliography	60	
Order Form	67	

EXECUTIVE SUMMARY

External auditing is promoted as a service that enables stakeholders to manage, control and prevent risks. However, a steady stream of audit failures shows that it also harms people. Audit failures are routinely implicated in the loss of jobs, homes, savings, pensions, taxes and investment. The institutionalisation of audit failures draws attention to the culture and values prevalent within major accountancy firms which are geared towards advancing their narrow economic interests, often at the expense of wider social interests.

Accountancy firms enjoy a state guaranteed monopoly of external auditing and insolvency markets. Yet no independent regulator regulates them. Major accountancy firms will do almost anything to make money. In pursuit of profits they operate cartels, launder money, devise tax avoidance/evasion schemes, bribe officials and obstruct inquiries into their affairs. They use external audits as a loss leader to sell other services. The internal organisation of accountancy firms encourages falsification of audit work. The absence of 'duty of care' to individual stakeholders affected by audits dilutes the economic incentives to deliver good audits. The longevity of auditor appointments encourages personal relationships with company directors. Frequently, audit staff are auditing their own former senior colleagues and partners, now enjoying a directorial position in a client company.

In everyday life, people encounter numerous varieties of auditors ranging from immigration control officers, Inland Revenue, Customs & Excise, Health and Safety inspectors and many more. In no case does the auditee appoint and remunerate the auditor as they do in company audits. The basic audit model fails because it expects one set of capitalist entrepreneurs (accountancy firms) to regulate another (company directors). Profits, income and appeasement of clients measure the success/failure of both. Serving the public interest does not form any part of this equation.

Legal, educational and regulatory environments could check such predatory practices, but they are weak. Accountancy trade associations, rather than an independent regulator, regulate accountancy firms. The main responsibility for the poverty of auditing practices rests with the Department of Trade & Industry (DTI) which has done little to check the anti-social practices of accountancy firms. Indeed, it colludes with the firms to protect and advance their narrow economic interests.

CHAPTER 1

DANGER: ACCOUNTANCY FIRMS AT WORK

In modern societies, people enter into transactions (e.g. investments, pensions, savings, food, and transport) with faceless strangers. There is a recurring danger that the strangers may be untrustworthy and may abscond with the resources and/or indulge in harmful activities. So to manage risks¹, people are increasingly encouraged to value surveillance technologies and place trust in socially accredited specialists with expert knowledges (Power, 1997). Following a 19th century spate of financial scandals, the state invested in systems of surveillance and external auditing came to be institutionalised as a trust engendering technology (Sikka et al., 1998). Auditing increasingly functions as a political technology enabling the state to regulate banks, insurance companies, pension funds and markets (Arnold and Sikka, 2001; Mitchell et al., 2001).

Auditing has been a real boon for accountancy firms. There are no state guaranteed monopolies for engineers, scientists, mathematicians, computer experts and other wealth creators, but audit work is reserved for accountants belonging to a handful of accountancy trade associations. Nearly 600,000 limited companies plus hospitals, universities, local authorities, pension funds, schools, trade unions, housing associations and charities need to have their books audited by an accountant. Not surprisingly, accountancy is an attractive career. Britain has around 250,000 qualified accountants, more than the rest of the European Union put together. Between 10% and 20% of all university graduates are making a career in accountancy. This huge investment in economic surveillance has produced neither superior corporate governance nor freedom from frauds, better protection for stakeholders or business accountability.

Today accountants rather than Parliament decides what counts as solvency, liquidity, asset, liability, equity, debt, income, expense, profit and loss. Their decisions affect pensions, wages, dividends, prices, jobs, taxes and the daily life of shareholders, creditors, employees, pension scheme members and other stakeholders. This huge social investment in economic surveillance gives accountants security of income, job and status. On the back of the state guaranteed market of auditing, accountancy firms have become consultancy supermarkets. Despite making decisions that affect the daily lives of people, accountancy firms are not required to publish any meaningful information about their affairs. To ensure public legitimacy, a President of the Institute of Chartered Accountants in England & Wales (ICAEW) said that

¹ 'Risk' is a fairly loose term. In everyday language 'risks' tend to be associated with hazards, dangers, threats or harms.

"there is an explicit responsibility to report publicly (whether or not required by law or regulation) incumbent on every economic entity whose size or form renders it significant. By economic entity we mean every sort of organisation in modern society, whether a department of central government, a local authority, a co-operative society, an unincorporated firm By significant we mean that the organisation commands human and material resources on such a scale that the results of its activities have significant economic implications for the community as a whole."

We consider that the responsibility to report publicly is separate from and broader than the legal obligation to report and arises from the custodial role played by economic entities"

Source: Accounting Standards Steering Committee, 1975, p. 15.

None of this has been followed by any concrete action. The ICAEW has opposed all calls requiring firms to publish any meaningful information about their affairs. Only scandals reveal anything about the composition of the audit team, standards of work, predatory practices, conflicts of interests, nature of the audit contract and their collusive relationship with company directors.

In the pre-Enron world, five secretive firms dominated the global accountancy scene. Their income is greater than the Gross National Product (GNP) of many nation states.

FEE INCOME OF ACCOUNTANCY FIRMS

FIRM	UK INCOME £millions	GLOBAL Income US\$ billions
PricewaterhouseCoopers	2,120	22.3
KPMG	1,160	11.7
Deloitte & Touche	796	12.4
Ernst & Young	626	9.9
Arthur Andersen	619	9.3

Sources: Accountancy, July 2001, p. 16; February 2002, p. 13.

In pursuit of profits, major accountancy firms conduct “consultancy audits”. They receive as much as 73% of their income from selling consultancy services to their audit clients (Accountancy, October 2001, p. 7). They hire company directors and management, create systems of internal control, director remuneration packages, transactions (e.g. tax figures), operate internal audits, form subsidiaries and design complex financial schemes, and then pretend to audit the same. In the name of efficiency, audit work is often falsified or not done at all (Willett and Page, 1996). Firms openly flout the rules on auditor independence (Securities Exchange Commission, 2000). The economic incentives for delivering good audits are weak. Unlike the producers of sweets and potato crisps, auditors do not owe a ‘duty of care’ to any individual stakeholder affected by their negligence. Despite major scandals, the Department of Trade and Industry (DTI) has never prosecuted any UK auditing firm for negligence.

Ordinary people are suffering from failures of accounting firms. Audit failures played a part in a crisis for 30,000 Maxwell pensioners (House of Commons Social Security Committee, 1992). They played a part in the closure of Polly Peck, valued at £1.7 billion, and the loss of 17,227 jobs (Mitchell et al., 1991) and facilitated losses to 11,000 shareholders of Sound Diffusion Plc (Department of Trade and Industry, 1991a). Auditors failed to note the frauds that led to the conviction of five officials of the Baptist Foundation of Arizona on 32 counts of fraud, racketeering and theft. 11,000 investors lost £400 million (Daily Mail, 2 April 2002). The US Senate’s report on the closure of the Bank of Credit and Commerce International (BCCI) concluded that auditors were a party to a “cover up” (US Senate Committee on foreign Relations, 1992, p. 276) and caused “*substantial injury to innocent depositors and customers [emphasis added] of BCCI*” (US Senate Committee on foreign Relations, 1992, p. 5). Audit failures were associated with the loss of 14,000 jobs and losses to over one million bank depositors with deposits of US\$1.85 billion.

In the aftermath of audit failures at secondary banks, property and insurance companies, in the 1970s, the UK taxpayer had to spend £3,000 million to bail out the ailing sectors (Reid, 1982). The frauds and audit failures at Barlow Clowes required the British taxpayer to spend £153 million in compensation to investors (Department of Trade and Industry, 1995; Parliamentary Commissioner for Administration, 1989). The real/alleged audit failures in the US Saving and Loans industry may have cost \$400-\$500 billion in bailouts (Pizzo et al., 1990). The collapse of Enron, the world’s largest bankruptcy, is associated with audit failures where the audit firm devised corporate structures, created numerous subsidiaries (including 900 offshore) and financial transactions. Numerous investors, employees and creditors lost their investment, pensions and savings. The

company routinely massaged its accounts to conceal liabilities and report high profits. Enron auditors, Arthur Andersen, performed consultancy services, including (since 1990) internal audits. As the regulators were poised to examine the Enron bankruptcy and Andersen audit failures, the firm shredded a number of relevant electronic and paper documents (Financial Times, 11 March 2002). The US Department of Justice (press release, 14 March 2002) charged Arthur Andersen with criminal conduct. On 15th June 2002, a federal jury convicted Andersen of obstructing justice by shredding key documents of its audit client, Enron.

Given the power and influence of major firms, their activities should be scrutinised and regulated by a powerful independent regulator. Instead, the UK government has delegated regulation to accountancy trade associations. This policy of appeasement has resulted in 23 overlapping regulators (see Appendix 1). Even then there is no independent complaints investigation procedure and no ombudsman to provide speedy and cost effective adjudication of complaints. None of the regulators owes a ‘duty of care’ to any individual affected by their activities. Unsurprisingly, audit failures are institutionalised and continue to damage the lives of ordinary people.

Almost every week, newspapers report some new incidence of audit failure, all brought to public attention by whistleblowers and investigative journalists or by victims of frauds rather than by accountancy firms, accountancy trade associations or any government department. The auditing industry’s standard response to audit failures is to blame someone else, claim that the failures are the work of ‘bad apples’, tweak auditing standards, codes of ethics, regulation and make calls for better training of accountants (Sikka and Willmott, 1995a). These tactics are designed to deflect attention away from the culture and values of accountancy firms. Failures are not just the result of ‘bad apples’; the ‘bad apples’ are the product of a rotten orchard, and the trees need a good shake. Accountancy firms are engaged in ‘dirty business’ and their power is unchecked because they colonised and captured the regulatory and political scene to protect their economic interests.

This monograph argues that the ability of accountancy firms to cause substantial injury to depositors, customers, employees, creditors, shareholders, pension scheme members and other stakeholders is, amongst other things, the product of their organisational values and cultures². The prime responsibility for scrutinising

² The term ‘culture’ is subject to considerable debate. Things in themselves rarely have any meaning. It is the participants who give meaning to practices and situations. In the context of this paper, ‘culture’ is understood as the production and exchange of meanings within an accountancy firm. It is constantly produced

the organisational practices of accounting firms and curbing their capacity to do social harm rests with the government, which granted them a monopoly of the external auditing and insolvency industries. However, successive UK governments have shown little willingness to undertake such investigations. They have delegated the responsibilities to the accountancy trade associations, which act as sponsors, promoters, defenders and regulators of the UK auditing industry (Sikka and Willmott, 1995a, 1995b). The auditing regulators pay little attention to the role of organisational practices and values in institutionalising audit failures and social harms.

This monograph is divided into seven further chapters. Chapter 2 argues that whilst society has made considerable investment in auditing technologies, auditing knowledge continues to fail. It fails because the knowledge base of auditing is unsound. It also fails because auditing firms are primarily profit seeking businesses. In their pursuit of profits, they bend the rules and engage in numerous questionable practices. Chapter 3 shows that in pursuit of money accountancy firms operate cartels, indulge in money laundering, tax evasion and bribery. They also exploit their labour force, threaten clients and use audits to sell other services. Chapter 4 shows whilst legislation continues to strengthen auditor's legal rights, auditors fail to meet their legal obligations. Despite laws, auditors walk away quietly from problem clients. They also reach prior arrangements with company directors and avoid giving meaningful answers to questions at AGMs. Chapter 5 shows that rather than ensuring that accountancy firms meet their social obligations, auditing regulators are very economical with information. We draw attention to research that has problematised auditor's claims of independence. Firms do not respect self-regulation. In pursuit of profits, they have no difficulty in flouting rules. Chapter 6 shows that major firms secure business by claiming to be 'global' organisations, but when their actions are called into question by international regulators, their claims of globalisation evaporate. Chapter 7 shows that since the late 1960s, the auditing industry has mediated public scrutiny by tweaking the regulatory arrangements, the ethical guidelines, the disciplinary processes and by issuing soothing reports which always promise major reforms. However, major reforms never take place. Through these tactics, self-regulation is retained and the auditing industry's accountability is organised off the political agenda. Chapter 8 concludes the monograph by suggesting some reforms.

and exchanged in personal and social interaction. Meanings also regulate and organise the conduct of daily life (Hall, 1997).

CHAPTER 2

THE SEEDS OF FAILURES

Auditing is frequently promoted as a risk management technology. The very idea of ‘risk’, in a modern context, assumes that nothing is preordained and fixed and that the social arrangements are the outcome of human action rather than the invisible hand of fate (Lupton, 1999). Modernity creates the feelings that future misfortunes, threats, harms, hazards and dangers can be prevented, controlled or managed by investment in suitable technologies, modes of government, forms of surveillance, accountability, bureaucracy, institutional structures and trust engendering technologies (Douglas, 1986; Giddens, 1991; Beck, 1992). Modernity encourages the belief that the social world can be controlled by investment in modes of objective knowledge and rational thinking and that the risks can be calculated and predicted.

Many of the risks associated with modern life cannot easily be seen, smelt, observed, or felt. So rather than relying upon local knowledges, traditions, habits, or observations, the construction of risks is mediated and regularised by reliance upon specialist knowledges and experts that people rarely meet or encounter in everyday life (Giddens, 1991). By appealing to their status, education and socially constructed credentials, experts seem to hold out the promise of certainty and bringing the future under control. People are encouraged to look to assumed experts to diagnose problems and offer advice. As a result, ‘risk’ analysis, risk management and surveillance is big business, providing employment for thousands of consultants, advisers, auditors and experts.

The limitations of expert knowledge are often highlighted by unexpected events (e.g. diseases, corporate failures) which show that the concepts and theories advanced by experts cannot adequately grasp reality. As modernity is accompanied by intense fractures and fragmentation of daily life, it also produces social conflicts. In societies marked by social divisions and antagonisms emanating from inequalities relating to class, gender, age, ethnicity, wealth and income, the significance and meaning of expert knowledge cannot be fixed in any permanent sense. The meanings are open to intense struggles, especially by those who claim to have a direct interest in promoting particular interpretations of risk objects and practices. The experts often deflect public criticisms by denouncing critics/victims and arguing that the public expects too much, or that they had been misled by someone else (Douglas, 1982).

In modern societies, expert knowledges and specialists reside in capitalist

organisations. These generate pressures to prioritise fees, income, profits and market shares over compassion, care and social responsibility. In pursuit of private gain, some organisations facilitate expertise that causes death and genocide (Black, 2001) and generally promote profit over people (Chomsky, 1999). In pursuit of private gains, food experts have sanctioned the consumption of unfit food (Schlosser, 2001; House of Commons, 2000). Financial experts have sanctioned the sale of undesirable pension schemes (House of Commons Treasury Committee, 1998). Accountants have laundered money (Mitchell, Sikka and Willmott, 1998). Auditors put appeasement of company directors above the interests of employees, pension scheme members and investors (Department of Trade and Industry, 2001). The reliance upon experts is double-edged. It oils the wheels of economy and society, but it also facilitates physical, economic and social injury to a large number of people and to society generally. The social production of wealth, certainty and regulation is systematically accompanied by social production of risks (Beck, 1992), but rarely by reflections upon the organisational values and practices of the assumed experts.

Concerns about risk and regulation are mirrored in the processes of auditing. There is a strongly held view that audit risks can be managed or minimised by the development of objective knowledge in the shape of probabilities and statistical sampling (for example, see Auditing Practices Board, 1995a, 1995b). Auditors are encouraged to make predictions about the future by using past accounting numbers and mathematical models (Altman, 1968; Altman and McGough, 1974; Auditing Practices Board, 1995c) and shield themselves from threats through insurance cover. Alternative forms of knowledge and social understandings have been driven off the educational schema and rulemaking considerations. No amount of sampling, analytical review, or predictive models can persuade auditors to reflect upon the social consequences of their actions. These technologies may help to minimise or direct audit effort, increase profits, and possibly protect audit firms/partners from the consequences of real/alleged audit failures. They rarely encourage reflections upon the negative social consequences of the organisational practices of accountancy firms.

Since company audits are performed by capitalist organisations, their success/failure is measured by fee income, profits, number of clients and market share. Within accountancy firms the emphasis is “firmly on being commercial and on performing a service for the customer rather than on being public spirited on behalf of either the public or the state” (Hanlon, 1994, p. 150). Accountancy firms enjoy a monopoly of the state guaranteed market of external auditing, but the procurement of clients and fee income is heavily dependent upon personal relationships with company directors who need to be persuaded to hire a

particular accountancy firm. Securing the office of the auditor is important because it enables the firms to sell lucrative consultancy services. Accountancy firms are part of an 'enterprise culture' that persuades many to believe that 'bending the rules' for personal gain is a sign of business acumen (Partnoy, 1997). Stealing a march on a competitor, at almost any price, to make money is considered to be an entrepreneurial skill, especially where competitive pressures link promotion, status, profits, markets and niches with meeting business targets.

The expansion of the entrepreneurial accountancy firm has not been accompanied by moral constraints that require consideration of the social consequences of their organisational practices. In such an environment, numerous practices are considered to be acceptable as long as they generate private profits. The 'failure' is not seen to be connected with using dishonourable, predatory or anti-social practices but in being exposed or caught, as it can damage the carefully cultivated veneer of respectability and professionalism and limit the possibilities of securing fees and profits. The likelihood of being caught and punished can stimulate reflections upon organisational practices. Such possibilities can be created by developing strong and effective regulatory arrangements. However, the state's ability to intervene is constrained by deregulationist ideologies that seek to limit its ability to monitor the internal practices of accountancy firms. The increasing reliance of political parties and governments upon private monies also constrains the state's ability to institute regulation when it is opposed by major businesses (Chomsky, 1999; Monbiot, 2000). Faced with such constraints, the state has delegated the regulation of auditing to accountancy trade associations. Following the Companies Act 1989, the accountancy trade associations regulate the auditing industry and investigate real/alleged cases of audit failures. They are expected to promote, defend, regulate and prosecute auditing firms. Yet they have no independence from the auditing industry. Rather than examining the organisational values and cultures giving rise to the audit failures the accountancy bodies individualise the failures (Joint Disciplinary Scheme, 1999). This way attention is deflected away from the organisational practices and values. In the weak regulatory environment, malpractices by accountancy firms go unchecked and audit failures remain institutionalised.

The remainder of this monograph draws attention to some auditing practices that offer insights into the organisational culture and practices of accountancy firms. These may help to increase profits and revenues, but are rarely accompanied by reflections upon their consequences for the welfare of audit stakeholders.

CHAPTER 3

MONEY, MONEY, MONEY

Paralleling a fateful remark of Gerald Ratner's to the effect that his shops sell 'crap', the chairman of Coopers & Lybrand (now part of PricewaterhouseCoopers) stated that "there is an industry developing, and we are part of it, in [accounting] standards avoidance" (Accountancy Age, 19 July 1990, p. 1). In this environment, firms will do almost anything to make a fast buck.

Double Digit Growth

An analysis of the fees paid by the FTSE 350 companies shows that only 27% of the fees paid to auditing firms are for audits (Accountancy, October 2001, p. 7). The consultancy income from some clients companies dwarfs the audit fees.

SOME EXAMPLES OF FEES PAID TO MAJOR AUDIT FIRMS

Company	Audit Firm	Audit Fee £m	Non-audit Fee £m
AstraZeneca	KPMG	2.14	9.31
BAE Systems	KPMG	3.03	16.21
BP Amoco	E&Y	18.70	34.20
British Airways	E&Y	1.25	4.07
CGNU	PwC/E&Y	6.70	43.00
Cable & Wireless	KPMG	2.70	17.00
Kingfisher	PwC	1.60	8.30
Lloyds TSB	PwC	4.00	32.00
Prudential	KPMG	1.90	18.80
J. Sainsbury	PwC	0.70	12.90
Scottish Power	PwC	1.50	11.40
Shell T & T	PwC/KPMG	11.40	31.50
Unilever	PwC	8.17	39.00
United Business	PwC	0.60	13.30
Vodafone	D&T	3.00	22.00
WPP	AA	3.70	6.40

Source: Accountancy, October 2001, pp. 72-73.

Audit gives accountancy firms easy access to company directors and a competitive 'inside' advantage over their consultancy rivals. They use audits as a

stall to sell executive recruitment, internal auditing, financial engineering, advice on mergers, downsizing, information technology, trade union busting and tax avoidance. For a fee, some firms will front shell companies, act as company directors, post boxes, print T-shirts and badges and lay golf courses. In pursuit of money they have become part of client companies and an extension of their finance and personnel departments. Instead of conducting 'independent audits', major firms offer 'consultancy audits' where the aim is to maximise the opportunities to sell consultancy services. All this has enabled them to achieve double-digit growth in profits and fees.

The carefully constructed veneer of professionalism conceals anti-social practices. They operate cartels to carve-up and control markets. Italy's competition authority has fined five leading accountancy firms £1.4m for anti-competitive practices between 1991 and 1998. The competition authority said it was fining Ernst & Young, PricewaterhouseCoopers (PwC was formed by the merger of Price Waterhouse and Coopers & Lybrand in 1998), Deloitte Touche Tomatsu, KPMG and Arthur Andersen for "consistently distorting market competition in Italian accountancy services", in particular by standardising prices co-ordinated to win clients. The firms admitted the charges and provided information which helped the Italian competition watchdog in its inquiry. The antitrust body said that it had taken this into account when imposing the fines (Financial Times, 22 Feb 2000, p. 8).

All over the world, ordinary people bear a higher share of tax to finance essential social infrastructure. This burden is increasing because a rich elite and many major corporations are avoiding taxes through novel avoidance schemes. Major accountancy firms charge around £500 per hour to devise elaborate schemes for tax avoidance. Accountancy firms, such as Arthur Andersen, KPMG, Deloitte & Touche, PricewaterhouseCoopers (PwC) and Grant Thornton have become multinational enterprises by advising companies on strategies for avoiding taxes (New York Times, 16 April 2002). A favourite tactic is to advise major corporations and the rich to escape to secretive offshore tax havens. Developing countries are losing some US\$50 billion due to tax avoidance. The UK taxpayer is estimated to be losing some £85 billion of tax revenues (Mitchell et al., 2002). Inevitably, ordinary people bear the cost of this by paying a higher proportion of their income in taxes and receiving worse public services.

With the rise of information technologies, deregulation, globalisation and easy transfer of money, accountancy firms have added money laundering to their list of profitable services. More than US\$1.6 trillion (roughly equivalent to the gross national product of France) is estimated to be laundered each year. Most of the

money comes from tax evasion, illicit trading, narcotics, bribery, smuggling, murder, slavery, pornography, robberies and prostitution. The illicit cash is turned into cybercash and transactions through shell companies and bank accounts. Accountants and lawyers, whose main concern is to secure private fees, front many of these. Their reward is around 20% of the money laundered. No one can launder large amounts of monies without the direct or indirect involvement of accountants. Accountants report less than 1% of the suspicious transactions reported to the National Criminal Intelligence Service (NCIS).

<u>TOTAL NUMBER OF DISCLOSURES MADE TO NATIONAL CRIMINAL INTELLIGENCE SERVICE</u>			
<u>YEAR</u>	<u>TOTAL DISCLOSURES</u>	<u>DISCLOSURES BY</u>	
		<u>ACCOUNTANTS</u>	<u>SOLICITORS</u>
1992	11,289	1	4
1993	12,750	2	4
1994	15,007	6	86
1995	13,710	38	190
1996	16,125	75	300
1997	14,148	44	236
1998	14,129	98	269
1999	14,500	84	291
2000	18,408	77	249

Source: Annual Reports of the National Criminal Intelligence Service.

Each year the NCIS complains that accountants do not report money laundering and suspicious transactions to it. In response, the DTI Ministers wring their hands and the accountancy trade associations make pious statements. The 'Proceeds of Crime Bill' proposes to make it a criminal offence for accountants not to report any suspicions or dubious transactions to the National Criminal Intelligence Service (NCIS), as well as the Inland Revenue. In response, the ICAEW claims that the "government plans to crack down on money laundering could be very damaging economically and pose a serious threat to the role of the accountant" (<http://www.accountingweb.co.uk>, 6 June 2001).

Evidence relating to the involvement of accountancy firms in money laundering is not hard to find. In a High Court case, Lord Justice Millett pointed the finger at accountants and accountancy firms and said that

"Mr. Jackson and Mr. Griffin knew of no connection or dealings between the Plaintiffs and Kinz or of any commercial reason for the Plaintiffs to make substantial payments to Kinz. They must have realised that the only function which the payee companies or Euro-Arabian performed was to act as "cut-outs" in order to conceal the true destination of the money from the Plaintiffs to make it impossible for investigators to make any connection between the Plaintiffs and Kinz without having recourse to Lloyds Bank's records; and their object in frequently replacing the payee company by another must have been to reduce the risk of discovery by the Plaintiffs".

"Mr. Jackson and Mr. Griffin are professional men. They obviously knew they were laundering money. It must have been obvious to them that their clients could not afford their activities to see the light of the day. Secrecy is the badge of fraud. They must have realised at least that their clients *might* be involved in a fraud on the plaintiffs".

Jackson & Co. were introduced to the High Holborn branch of Lloyds Bank Plc. in March 1983 by a Mr Humphrey, a partner in the well known firm of Thornton Baker [now part of Grant Thornton]. They probably took over an established arrangement. Thenceforth they provided the payee companies... In each case Mr Jackson and Mr Griffin were the directors and the authorised signatories on the company's account at Lloyds Bank. In the case of the first few companies Mr Humphrey was also a director and authorised signatory".

Source: High Court judgement in *AGIP (Africa) Limited v Jackson & Others (1990) 1 Ch. 265 and 275*; also see Mitchell et al., 1998.

In the above case, 27 separate companies were used to launder money, making it difficult to trace the source and destination of the proceeds. The paper trail went from Tunisia, London, the Isle of Man and Jersey to France and beyond. Most of the companies never traded but millions passed through their bank accounts. Accountancy firms collected fees for forming, operating and liquidating the shell companies. Despite the very clear and strong court judgement, there was no independent investigation or inquiry. The ICAEW and the UK government did the usual whitewash. Their main priority, as always, was to shield accountancy firms and their partners (Mitchell et al., 1998). Not surprisingly, money laundering is on the increase and accountancy firms don't bother to report suspicious transactions to the authorities.

To maintain their growth in profits, accountancy firms constantly need to find new ways of making money. Anything and everything is commodified to make money. Some firms have little hesitation in bribing officials to ensure that their 'private' interests triumph over the wider social interests.

“In 1996, the US regulators concluded a case involving the bribery of bank officers in U.S. and foreign banks in connection with sales of emerging markets debt, transactions that earned millions for the corrupt bankers and their co-conspirators. In this case, a private debt trader in Westchester County, New York, formerly a vice president of a major U.S. bank, set up shell companies in Antigua with the help of one of the **“big-five” accounting firms**. Employees of the accounting firm served as nominee managers and directors. The payments arranged by the accounting firm on behalf of the crooked debt trader included bribes paid to a New York banker in the name of a British Virgin Islands company, into a Swiss bank account; bribes to two bankers in Florida in the name of another British Virgin Islands corporation and bribes to a banker in Amsterdam into a numbered Swiss account” [emphasis added].

Source: Evidence by Robert Morgenthau, New York District Attorney, to the Permanent Subcommittee on Investigations on 18 July 2001 (http://www.senate.gov/~gov_affairs/071801_psimorgenthau.htm)

The shell company in the above case went under the name of Merlin Overseas Limited. There was no actual physical business in Antigua, named Merlin. It consisted of little more than a fax machine in a Caribbean office of Price Waterhouse (New York Daily News, 10 January 1999). “This accounting company was complicit”, said Robert Morgenthau, the Manhattan district attorney. “They facilitated hiding of bribes that were paid to bank officers, and they provided the officers and directors for those phoney companies”. Morgenthau prosecuted the rogue at the centre of the scheme but could not put his hands on Price Waterhouse. The district attorney’s office asked Price Waterhouse in Manhattan for help in reaching the people behind Merlin, but the help was not forthcoming. They were told that the Price Waterhouse in Antigua is not the same legal creature as the one in New York.

All over the world major accountancy firms are facilitating anti-social activities. They obstruct inquiries into frauds and fiddles and shield money launderers and fraudsters.

“In 1996, the U.S. Department of Justice came into possession of a tape

containing computerised records of a defunct Caymans bank, Guardian Bank and Trust Company. The bank was started by John Mathewson, a businessman from Illinois. Years after opening a numbered Swiss bank account whilst vacationing in the Caymans, he was persuaded by a Caymans banker to start his own bank. According to Mathewson, his application for a bank licence asked for little more than his name, address and previous bank history. The bank was set up and used to launder money for its depositors, 95% of whom were U.S. residents. Fake invoices to enable US citizens and corporations to disguise deposits were used. The government of Cayman sought to block the release of banking information and refused to help the FBI to decode computer records. The official Cayman liquidators of the bank (two partners in **another major world-wide accounting firm**) brought a suit in the U.S. District Court in New Jersey seeking the return of the computer tape to the Caymans. In their brief, the liquidators argued that disclosure of the contents of the records to, among others, the U.S. Internal Revenue Service would “Have a significant negative impact on the integrity, confidentiality, and stability of the financial services industry of the Cayman Islands. The confidence of the offshore financial community in the privacy afforded to legitimate account holders of Cayman Islands offshore banks is at the heart of the Territory's financial services industry and economy, as a whole. Thus, not only would the Bank be irreparably injured by the government's retention of the Tape, but the international bank and Eurocurrency industries of the Cayman Islands (and, indeed, the economy of the Territory), could suffer irreparable injury as well”. After decoding the tape without the help of the Caymans government, the US authorities discovered that the Guardian Bank's U.S. depositors had \$300 million offshore, hidden from tax authorities, litigants and creditors. In view of his help to the US authorities, Mathewson was given a five year suspended prison sentence and said, “I have no excuse for what I did in aiding US citizens to evade taxes, and the fact that every other bank in the Caymans was doing it is no excuse”.

Source: Evidence by Robert Morgenthau, New York District Attorney, to the Permanent Subcommittee on Investigations on 18 July 2001 (http://www.senate.gov/~gov_affairs/071801_psimorgenthau.htm); also see The Times, 4 August 1999, p. 16; Mitchell et al., 2002.

The Pursuit of Private Interests

The Enron scandal has shown that major accountancy firms exert pressures on partners and senior staff to increase revenues and profits. Those doing that are rewarded with status, bonuses and salary increments. Some firms intimidate audit clients in an effort to sell consultancy work. Angered by a client who used the

services of an independent consultancy company to value its brands for accounting purposes, the audit firm threatened the client suggesting that audit costs and 'problems' would rise if the independent consultancy company was used in preference to the firm's consultancy division (Accountancy Age, 14 February 1991, p. 1 and 17; Accountancy, March 1991, p. 11). The consultancy company complained to the ICAEW by arguing that "We find attempts to cajole clients into using consultancy services by threat of "problems" exceptionally seedy and unpleasant" (Accountancy Age, 14th February 1991, p. 17). The ICAEW did its usual whitewash.

A myth promoted by the accountancy industry is that the purchase of auditing and non-auditing services from the same firm somehow results in lower costs. Such myths are not supported by research (Simunic, 1980, 1984). This shows that when management invite competitive tenders, shop around and purchase auditing and non-auditing services from two separate firms, they get a lower price. As Simunic (1984) concludes, "audit fees for clients who purchased MAS [Management Advisory Services] from their auditors are higher than those of clients who did not do so" (p. 699).

Audits have long been used as loss-leaders to secure non-auditing work (Accountancy Age, 6 June 1991, pp. 1 and 4). Some firms have been offering free audits in the hope of picking up lucrative consultancy work (Accountancy Age, 20 June 1991, 1; Accountancy Age, 24 October 1991, p. 1). Lowballing is rife, with the big firms sometimes undercutting the medium-sized firms by as much as a third (Accountancy Age, 9 May 1991, p. 1; Accountancy Age 23 May 1991, p. 1; Accountancy Age, 9 January 1992, p.1). Price Waterhouse (subsequently part of PricewaterhouseCoopers) undercut the incumbent auditor of RAC by nearly 50% to secure the audit. Outgoing auditors, BDO Stoy Hayward, claimed that "We believe that this demonstrates a determined approach to price their audit work on a predatory basis so as to secure an appointment which might enable them to introduce higher priced consultancy services to RAC in due course" (Accountancy, June 1995, p. 13). As audit quality is neither visible to the public nor monitored by an independent regulatory agency, poor work only comes to the surface when an inquiry follows a company collapse/fraud or some investigative journalist pursues a story.

To maximise profits, firms impose tight time budgets on audit staff even though time constraints have played a major part in audit failures and incompleteness of audit work (Department of Trade and Industry, 1995). The time budgets are squeezed in the hope that audit teams will work free on evenings and week-ends to finish the work (for examples see, Accountancy Age, 24 March 1994, page 1;

Accountancy Age, 24 March 1994, page 1; The Times, 2 November 1995, p. 30). Fearful of losing their jobs and study leave, some oblige, but large numbers of audit trainees either use short-cuts, irregular practices or resort to falsification of audit working papers (Otley and Pierce, 1996). A survey by Willett and Page (1996) found that due to time pressures a large proportion of audit staff rejected awkward looking items. They accepted doubtful audit evidence, failed to test the required number of items in a sample, or simply falsified the audit working papers to give the impression that the work has been done. Such practices were carried out by senior and junior members of the audit teams. As the audit review process cannot completely reperform the audit, irregular audit practices rarely come to light.

In this environment of tight time budgets, competition and pursuit of higher profits, auditing firms look for ways of achieving efficiency. One of the common practices is to use checklists for controlling, planning and recording an audit. Such devices standardise audits and also make the process much more mechanical, predictable and possibly boring. The checklist mentality encourages irregular practices. In a radio programme (BBC Radio 4 – File on Four, 9 October 2001), an auditor with ten year experience said,

“If you pitch for an audit of certain value, obviously you have to try and do it within that price, so you skip lots of corners. I mean, you’ve got lots of checklists to fill-in – have you seen this? You just end up ticking ‘yes I’ve seen this, I’ve seen this,’ even though you haven’t So you end up with piles of checklists on your audit working papers, which basically are a complete fabrication, because you actually haven’t done the work. It’s so easy to just sit there and fill in checklists, even back in your hotel room, not even at the client’s premises, just so that when the partner rings up the next morning and says, ‘I hope you’re at least three quarters of the way through the audit’, you can say, ‘Yes, I am.’ The public doesn’t know what an auditor actually does. They don’t know the mechanics of an audit, so they are not aware of how much work has actually gone on to verify and authenticate the figures in the accounts. If the public were aware of, you know, sometimes how little work goes on, I think they’d be quite surprised and would be less inclined to take a clean audit report as being gospel that the accounts are actually accurate”

In folklore, the final audit opinion should be based upon the audit evidence collected and evaluated. However, in practice the economic interests of auditing firms, including the desire to sell non-auditing services, often prevail. According to an auditor,

“There can be various times when you’d want to qualify an audit, when you are not happy with things. The partners or partner responsible would be less inclined than yourself to qualify the report, mainly because they want the continuing business, or they already have a relationship with the client, or to keep the client on board, because there’s other aspects to the job as well, not just the audit. There’s also the accounts, all the directors’ tax returns, there might be a lot of tax planning and financial planning services going on as well, and management consultancy. All those sort of things are being provided to the client, which really ruins any independence you’ve got as far as being an auditor is concerned, because of all the background services that are also being provided. So there’s enormous pressure not to qualify the report, because you don’t want to lose the client.

[An example] The client was being very uncooperative indeed about stock, wouldn’t give us any stock records or stock level, and indicated that cooperation would only be given once he was aware of what our draft profit figures were. I told the partner that this was unacceptable and really we should qualify the report. However, the partner and the client were friends and, following, I suspect, a dinner or a drink or whatever, I was informed by the partner that this particular stock figure had been agreed and that there would be no qualification on the report. I have to say I was very unhappy about that, because it was obvious that the figure couldn’t be validated in any way. [Reporter: So they just went out to dinner together and cooked the books?]. Yes, you could say that. They basically agreed a figure which was put in the accounts, and the audit was signed off. In a sense they’re defrauding anyone that’s lent money to them, you know, their bankers, obviously the creditors, people doing business with them. Obviously also the Inland Revenue. If the tax liability is based on the accounts and those accounts are incorrect – for whatever reason – the correct liability is not being collected”

Source: BBC Radio 4 – File on Four, 9 October 2001.

The public is encouraged to believe that audits are conducted and supervised by experienced individuals. The DTI report on the collapse of Rotaprint plc found that

"The [audit] manager had no previous knowledge of the client. The remaining members of the audit team comprised an unqualified senior who had worked as a junior on the audit and four junior trainee accountants. The junior trainees were all at the same level of experience having joined Arthur Young [now part of Ernst & Young] some months earlier The audit team was therefore composed of

relatively inexperienced trainees led on a day-to-day basis by an unqualified senior"

Source: Department of Trade and Industry, 1991b, p. 46.

The public is encouraged to believe that auditors collect relevant and reliable evidence form their opinion. The reality is that in pursuit of profits, auditors do not always bother with such niceties. The DTI report on the collapse of London United Investment concluded that

"It was a mistake by KPMG not to have obtained third party confirmations it was a conscious decision by KPMG not to obtain third party confirmations We disagree with this decision"

Source: Department of Trade and Industry, 1993a, p. 281.

The public is encouraged to believe that auditors consider the accounting implications of all material transactions before signing the audit report. The DTI report on irregularities at Edencorp Leisure plc reported that

"Ernst & Young as auditors of the group signed an unqualified audit report on Edencorp's 1989 group accounts without apparently considering the accounting implications of the significant invoice issued We are therefore surprised that the accounting treatment adopted for the transaction was given so little attention by the finance director and auditors".

Source: Department of Trade and Industry, 1993b, p. 47.

A 300 page report on the collapse of Vehicle and General, which insured some 10% of Britain's motorists, was highly critical of the auditor's failure even to perform basic arithmetical checks on financial statements. For instance, an investment of £82,040 was shown as £820,040, but was not spotted by the auditors (Department of Trade and Industry, 1976a). Major audit deficiencies were also exposed by the report on London and County Securities (Department of Trade and Industry, 1976b). The company had entered into illegal share dealings and there were also fraudulent transactions between the company, directors and their families. The report described the company's accounts as "misleading to a material extent" (para 234) and criticised poor auditor performance.

The commercial considerations have persuaded auditing firms to remain silent

about questionable clients. For example, in January 1990, BCCI pleaded guilty to charges of money laundering (United States, Senate Committee on Foreign Relations, 1992, p. 61), but this did not prompt its auditors, Price Waterhouse, to resign or qualify the accounts. In pursuit of fees, accountancy firms accept and retain clients with ‘danger’ written all over them. For example, Coopers & Lybrand (now part of PricewaterhouseCoopers) accepted Robert Maxwell as a client even though he had previously been described as a person “who cannot be relied upon to exercise proper stewardship of a publicly-quoted company” (Department of Trade and Industry, 1973, 1972, 1971a). From 1972 (almost a year before the publication of the final damning DTI report) Coopers & Lybrand became auditors and business advisers to most of the Maxwell controlled companies and pensions funds. Maxwell who committed suicide, in November 1991, systematically plundered the pension funds to the tune of £458 million (House of Commons Social Security Committee, 1992). Some parts of the Maxwell empire did not keep proper accounting records but auditors continued to issue unqualified audit reports. The DTI inspectors’ report showed that the relationship between the audit firm and Maxwell was close. The appeasement of Maxwell was a major priority for the audit team (Department of Trade and Industry, 2001).

Some auditing aspects of the Maxwell debacle were examined by the Joint Disciplinary Scheme (JDS). Its report (Joint Disciplinary Scheme, 1999) concluded that the audit firm “lost the plot”, “got too close to see what was going on” and “failed to consider whether there was evidence of fraud, other irregularities, defaults or other unlawful acts” (The Times, 3 February 1999, p. 21; Financial Times, 3 February 1999, p. 10; The Observer Business, 7 February 1999, p. 6; Daily Mail, 27 May 1999, p. 5). The audit firm and its partners admitted 57 errors of judgement, including inadequate work, incompetent performance, undue acceptance of management representations, deficient consideration of the interest of third parties and deficient partner review³ (Chitty, 1999). Despite rules and regulations about auditor training, one of the partners claimed that he had never encountered fraud before. In response, the JDS individualised audit failures. Rather conveniently, most of the blame was allocated to an audit partner who died (in 1996) whilst the JDS was making its inquiries. The organisational values of the audit firm were not investigated.

Summary and Discussion

Accountancy business is big business. Concerns about efficiency, accountability,

³ The omissions and oversights were enough to persuade one commentator to conclude that “what in a working-class occupation would be seen as blatantly corrupt, in a middle class one is seen as a badge of pride” (Jenkins, 1999).

stewardship and primacy of private property rights encourage social investment in surveillance systems, such as accounting and auditing. Capitalist enterprises legitimise their operations by audits and people are encouraged to believe that the published information is somehow reasonable and fair. Auditors are often portrayed as watchdogs. Such images have enabled accountancy firms to secure state guaranteed monopolies of auditing and insolvency industries, but without a 'duty of care' to stakeholders affected by their actions. These monopolies are regulated by accountancy trade associations rather than by an independent regulator. In such an environment, accountancy firms make profits by heaping misery on others. To make profits, accountancy firms have been placing thriving businesses into receiverships and liquidation (Cousins et al., 2000). Ordinary people have lost their homes, jobs, businesses and savings whilst firms collect fees for many years.

The world of insolvency and auditing are dominated by a handful of secretive firms who publish little meaningful information about their affairs. They operate cartels, all with a view to making private gains and disadvantaging the wider public. They have added money laundering, bribery and obstruction of legitimate inquiries to their trade. Upon discovery of audit failures and abuses of insolvency services, some may expect one major firm to give evidence on the incompetence of another. But the pursuit of profits has created new brotherhoods of deceit and silence. In November 1998, the New Zealand case of *Wilson Neill v Deloitte - High Court, Auckland, CP 585/97, 13 November 1998* revealed that "The major accounting firms have in place a protocol agreement promising none will give evidence criticising the professional competence of other Chartered Accountants" (reported in the (New Zealand) Chartered Accountants' Journal, April 1999, p. 70). In an ideal world, the regulators would step in and tackle the institutionalised corruption of the accountancy industry. But accountancy firms live in a world regulated by accountancy trade associations. As our investigation of accountancy firm involvement in money laundering showed (Mitchell et al., 1998), accountancy regulators are primarily concerned with shielding accountancy firms rather than tackling the abuses.

CHAPTER 4

SILENCE PLEASE: AUDITORS AT WORK

Accountancy firms have a long history of “disclosing considerably less than what they actually know” (Woolf, 1986, p. 511). Audit failures draw attention to

“the ease with which eminent firms of auditors turned a blind eye on the wholesale abuse by client company directors of [legal] provisions. [The directors] operated these public companies for the principal benefit of themselves and their families; and most regrettable of all, on the virtual complicity of their auditors, whose efforts are seen to have amounted to a whitewash at best, and a fatuous charade at worst”.

Source: Woolf (1983).

Such suspicions are further supported by the practices of resigning auditors. Since the UK’s Companies Act 1976 (now consolidated into the Companies Act 1985), resigning auditors have been required to make public statements, addressed to shareholders and creditors of companies, to draw attention to the circumstances, if any, of their resignation.

Section 394(1) of the Companies Act 1985 states that “Where an auditor ceases for any reason to hold office, he shall deposit at the company’s registered office a statement of any circumstances connected with his ceasing to hold office which he considers should be brought to the attention of the members or creditors of the company, or if he considers that there are no such circumstances, a statement that there are none”. Such legal requirements were developed in the aftermath of corporate collapses and scandals where the silence of the auditors was considered to be detrimental to the interests of the stakeholders (Dunn and Sikka, 1998).

The Nelsonian Touch

This legislation on auditor resignation was introduced in the aftermath of the frauds at Pinnock Finance Group (DTI, 1971b) where the “asset figures in the balance sheets were not merely unrealistic but blatantly false” (p. 249). The auditors were described as “tame and negligent” and decided to walk away quietly. The provisions of the Companies Act 1976 were designed to “strengthen the position of auditors” (Hansard, House of Lords Debates, 23 March 1976, col. 550.), and particularly “strengthen the hand of the weaker brethren” (Hansard, House of Lords Debates, 23 March 1976, col. 578). The legislation is

accompanied by immunities from 'libel'. As a Minister put it, "unless the auditor uses a statement for some improper purpose - for instance, he is malicious in the legal sense - no person who is criticised will be able to sue him successfully for libel" (Hansard, House of Lords Debates, 5 April 1976, col. 1488). The aim of the legislation was to "give a strong auditor a very powerful and effective threat in the event of a dispute with the directors and will force even a weak auditor to face up to his responsibilities as he will no longer be able to evade a difficult situation by quietly resigning and saying nothing" (Hansard, House of Lords Debates, 23 March 1976, cols. 554-555).

Despite a proliferation of auditing standards and ethical statements, auditors remain reluctant or unwilling to discharge their obligations (Dunn and Sikka, 1999). Consider the case of the Queens Moat Houses Plc, once the third largest hotel chain in the UK. Through an aggressive acquisition policy, its profits grew from £24.8 million in 1987 to £94.1 million in 1990. The company's accounts carried unqualified audit reports until 1991. In 1993, just a week before its 1992 financial statements were to be published, the company asked (on 31st March 1993) the London Stock Exchange to suspend trading of its shares (The Times, 1 April 1993, p. 23). Major banks were asked to devise a financial package to rescue the company (The Times, 8 April 1993, p. 25). Grant Thornton were asked to investigate the company's affairs. This investigation revealed (April 1993) that the company was likely to report a substantial loss (The Observer, 23 May 1993, p. 30). A large number of directors either resigned or left.

Amidst these events, on 18 May 1993, Queens Moat Houses auditors, Messrs Bird Luckin, resigned and stated, "we confirm that there are no circumstances connected with our resignation which we consider should be brought to the notice of the members or creditors of Queens Moat Houses plc".

The company's financial statements for the year to 31st December 1992 were finally published on 29 October 1993. Its 1991 pre-tax profit of £90.4 million was restated as a loss of £56.3 million. The £146.7 million difference included £50.9 million of depreciation that the group had not previously provided for and maintenance expenditure which had been capitalised. Other changes related to overstatement of profits on fixed sales, expenses which had been capitalised and misclassification of finance leases. Whilst analysts were predicting a profit of some £90 million for 1992, the actual published accounts revealed a pre-tax loss of £1.04 billion. Much of it was due to exceptional items and a write-down of property values. The 1992 balance sheet showed net debt to be £1.17 billion and a negative net worth of £388.9 million.

For the two previous years the company had been operating with virtually no financial controls (Financial Times, 30/31 October 1993, p. 8). It was alleged that the company had paid unlawful dividends for 1991, 1992 and 1993 (Financial Times, 30/31 October 1993, p. 1; The Observer, 31 October 1993, p. 2). The finance director's report explained that "there were no monthly consolidated management accounts to enable the board to monitor the progress of the group". In particular there were minimal group cash forecasts and no clearly defined treasury function. It was reported that one of the company's directors was a former partner of the audit firm. On 12 November 1993, the Department of Trade and Industry appointed inspectors under section 432 of the Companies Act 1985 to investigate the affairs of the company. The resulting report remains unpublished.

Take another example of MTM Plc, once the second largest fine chemicals company in the UK. In 1992, it collapsed with debts of £250 million (The Independent, 4 February 1997, p. 16). The company had issued two profit warnings and its share price plummeted from 286 pence to 26 pence (Financial Times, 1 May 1992, p. 20). There were considerable disagreements between auditors, BDO Binder Hamlyn, and the Board and the announcement of the 1991 financial results was delayed. In March 1992, Richard Lines, MTM's chairman and founder, resigned over disagreement with the auditors "over application of accounting policy" (Financial Times, 11 March 1992, p. 11). An internal report prepared by auditors suggested that the company boosted its sales and profits by "incorrectly recorded" transactions (Financial Times, 14 May 1992, p. 22). In May 1992, it was reported that MTM was "co-operating fully with the SFO [Serious Fraud Office] and the North Yorkshire police in an investigation being carried out concerning matters relating to that shortfall" (Financial Times, 14 May 1992, p. 22).

MTM's auditors, BDO Binder Hamlyn, gave an unqualified audit opinion (dated 5th June 1992) on the financial statements for the year to 31st December 1991. On 8th September 1992 they resigned and stated that "There are no circumstances connected with our resignation which we consider should be brought to the attention of the members or creditors of the company".

The very next day, the company announced an interim loss of £28 million and its new chief executive claimed that the previous year's accounts were materially overstated (Financial Times, 10 September 1992, p. 20). The new chief executive sought to restructure the company and looked for a substantial cash injection. Price Waterhouse took over the audit. The firm's first audit report, dated 28 April 1993, related to the financial statements for the year to 31st December 1992. It

referred to the fact that “the company is co-operating with the Serious Fraud Office and the North Yorkshire Police in relation to an investigation being carried out concerning matters relating to the profit shortfall announced in the 1991 Reports and Accounts ...”.

The SFO inquiries continued in 1993 (Financial Times, 10 April 1993, p. 10) and in 1994. Richard Lines and Thomas Baxter, another former MTM director, were formally charged with false accounting, conspiracy to commit false accounting or furnish false information, and making false and misleading statements under the Financial Services Act. It was alleged that they recorded bogus transactions for 1990 and 1991 in order to meet profit forecasts. According to the prosecuting QC, the directors, "assisted by others, cooked the books, in order to give the impression that the company was a good deal more profitable than was, in fact, the case" (Financial Times, 4 February 1997, p. 12). Amongst other things directors sold company's plant and machinery to a supplier for a profit of £700,000 with an agreement to repurchase the assets so that there was no net cost to the supplier. Both former directors were convicted of fraud and Richard Lines was sentenced to two years imprisonment and Thomas Baxter to six months (Serious Fraud Office Report, 1996/97). In relation to the auditors, the judge said, "It may be that BDO had become far too cosy with MTM" (Financial Times, 4 February 1997, p. 12).

Auditors Will Fix It

Auditors have considerable statutory rights to communicate their concerns to shareholders and creditors. Ever since the Companies Act 1948 (Section 160), auditors have been empowered to speak at all Annual General Meetings (AGM) and express their concerns about anything relating to financial statements. However, auditors appear to be more concerned to appease company directors, their effective paymasters. Consider the case of Ramor Plc, a company audited by Price Waterhouse (now PricewaterhouseCoopers). To prepare for the possibility that someone attending the AGM might ask searching and unwelcome questions, the auditors reached a prior agreement with the company to be ‘economical with information’, as evidenced by a letter exchanged between the chairman of the company (Mr. Smith) and the Price Waterhouse audit partner (Peter Ainger). The letter said,

Dear Mr. Smith,

As arranged I am writing to let you know in advance of the Annual General Meeting on 26 July the replies I will give if I am asked by a shareholder for the reasons why my firm is not seeking re-election as auditors. If no questions are asked, then of course, no further information in addition to that contained in the Annual Report need be provided.

However, if a shareholder asks further information I propose to reply as follows:

“In recent years we have experienced certain difficulties in obtaining necessary information for our audit and being sure that all relevant explanations have been provided to us. In the final outcome we have been satisfied that we have received all such information and explanation; otherwise this would have been reflected in our audit report. However the situation created by these difficulties caused us to agree with the directors that we would not seek re-election at this meeting, a step we are permitted to take under the provisions of the Companies Act.”

If there should be a follow-up question asking for more information about the difficulties referred to in the foregoing statement I would propose to reply as follows:

“There was no one matter which in itself caused us to reach this agreement with the directors. In view of this, there is nothing more that can be added to the answer that has already been given”

I would not intend to give any more information nor to respond to any other question”.

Yours sincerely
PL Ainger

Source: Department of Trade and Industry, 1983, p. 283.

Following allegations of frauds, the Department of Trade and Industry appointed inspectors (Department of Trade and Industry, 1983). The interim report⁴ of the inspectors concluded that,

⁴ Peter Ainger acted as an inspector to investigate the affairs of Gilgate Holdings Limited. At the same time, his role in the audit of Ramor Investments was being investigated by other DTI inspectors. The DTI eventually contrived to suppress the final report relating to Ramor Investments (see Sikka and Willmott, 1995).

“Price Waterhouse's conduct as regards the non-executive directors and incoming auditors is indefensible” (p. 286).

"Price Waterhouse's acceptance of the position and of the manipulation is both surprising and disturbing" (p. 79).

“at the AGM itself Mr. Ainger [Price Waterhouse partner] despite having notice of questions, answered them in terms which gave the shareholders less than the full picture and conveyed an impression of certainty which was not justified” (p. 278) .

"..... we have no hesitation and have no doubt that Price Waterhouse attempted to play down the situation" (p. 285).

The public facade was that “By mutual agreement our Auditors Price Waterhouse & Co. are not seeking re-election” (DTI, 1983, p. 283), but the inspectors concluded, “there was nothing mutual in Price Waterhouse’s decision to go” (p. 284). The DTI inspectors criticised Price Waterhouse for resigning the audit and going too quietly (Department of Trade and Industry, 1983, chapter 14).

Summary and Discussion

Accountancy firms are adept at keeping quiet. They pick up fees whilst the public picks up the cost of lost jobs, savings and investments. After major scandals, the powers and rights of auditors are strengthened, but little attention is paid to the culture of accountancy firms. In pursuit of private profits, accountancy firms do not really want a reputation of being awkward or public-spirited. They do not want to upset company directors as this can restrict their ability to sell lucrative consultancy services. Auditing firms are more concerned about protecting their flow of profits than answering questions about their own and/or corporate conduct, which could arguably enable some stakeholders to manage their risks and call organisations to account. Neither the DTI nor any auditing regulators monitors compliance with the spirit of the auditor resignation legislation. Indeed, the DTI has failed to publish statistics about auditor resignations.

Accountancy firms continue to devise strategies to thwart questions at AGMs and the provision of meaningful information. All this has been documented in DTI inspectors’ reports. Yet successive governments and regulators have indulged the auditing industry and have failed to require the firms to open their working papers and files to stakeholders affected by their conspiratorial silence.

CHAPTER 5

STRUCTURAL AND CULTURAL PROBLEMS

Accountancy firms use audits as a market stall to sell non-auditing services (Accountancy, June 1995, p. 13; Mitchell and Sikka, 1993). Unlike other auditors (e.g. Inland Revenue, Customs & Excise, Health and Safety Executive), financial auditors hire company directors, value assets, create business transactions, internal control systems, accounting systems, perform internal audit functions and then claim that they can somehow audit the same without any detrimental effect on their independence.

Rather than ensuring that auditors act exclusively as auditors, the regulators are economical with information. For example, the ICAEW (a regulator of the auditing industry) Deputy President and PwC partner, Peter Wyman, claimed that "Independent investigations have not shown the provision of consulting services to have been the cause, or even a contributory cause, to any audit failure". (Financial Times, 21 January 2002, p. 14). Such claims are easy to make, as auditing firms are some of the most secretive organisations. Their files are not available to audit stakeholders and an independent regulator does not regulate them. Nevertheless, the assertion is untrue. On occasions authoritative investigators have associated audit failures with the sale of consultancy services to audit clients.

Auditors of Roadships were criticised for their failure to adequately check the amounts for creditors, accruals, purchases and profit forecasts (DTI, 1976c). The audits were not independent since auditors acted as consultants for the company. The inspectors (one of whom is usually a partner from a major accountancy firm) argued that

"Independence is essential to enable auditors to retain that objectivity which enables their work to be relied upon by outsiders. It may be destroyed in many ways but significantly in three; firstly, by the auditors having a financial interest in the company; secondly, by the auditors being controlled in the broadest sense by the company; and thirdly, if the work which is being audited is in fact work which has been done previously by the auditors themselves acting as accountants."

Source, DTI, 1976c, para 243.

After examining the quality of audits performed by auditors who also provided non-auditing services, the inspectors concluded,

"We do not accept that there can be the requisite degree of watchfulness where a man is checking either his own figures or those of a colleague. for these reasons we do not believe that [the auditors] ever achieved the standard of independence necessary for a wholly objective audit."

Source: DTI, 1976c, paras 249 and 250.

The DTI inspectors' report on Hartley Baird found that the company was having difficulties in repaying loans. But the financial problems were covered-up by manipulation of the accounts. The report stated that the auditors were ineffective because of their close connections with company directors and suggested rotation of auditors (DTI, 1976d).

The Department of Trade and Industry (DTI) inspectors' report on Burnholme and Forder (DTI, 1979) was critical of audit work and once again felt that auditor independence was compromised by the provision of non-auditing services to audit clients. They concluded,

"in our view the principle of the auditor first compiling and then reporting upon a profit forecast is not considered to be a good practice for it may impair their ability to view the forecast objectively and must endanger the degree of independence essential to this work"

Source; DTI, 1979, p. 271.

In 1978, the collapse of the Grays Building Society reminded people of the ineffectiveness of external auditors. The resulting investigation (Registry of Friendly Societies, 1979) found that the same firm had been auditing the building society for nearly forty years. Its partners became friends of directors and frequently took holidays together. The auditors failed to perform the simplest of checks and did not spot frauds of more than £7.1 million, carried out over a period of some forty years. The frauds only came to light when the chairman committed suicide. The report was highly critical of auditors and noted that their 'independence' had been compromised by their longevity in office and the personal relationships with company directors which had developed as a consequence. Similar issues were to be raised again by audit failures at Polly Peck, Levitt and Maxwell where the same firm conducted audits for many years.

The DTI report on Kina Holdings (DTI, 1981a) criticised auditors and noted that

the same firm had been providing auditing and non-auditing services to a major quoted company for a number of years. This relationship resulted in a considerable part of the firm fee income coming from one client. Audit failures continue to raise questions about auditor independence. For example, Stoy Hayward acted as auditors and consultants to Polly Peck for a period of fifteen years. The firm always issued unqualified audit opinions.

The House of Commons Select Committee on Social Security recommended that pension fund auditors should not be allowed to perform non-auditing services for their audit client (Accountancy Age, 12 March 1992, p. 1; Accountancy, April 1992, p. 18). Such recommendations followed consideration of frauds perpetrated by Robert Maxwell, an episode which once again raised questions about the desirability of auditors auditing the balance sheet figures that they themselves had created. In 1991, the Maxwell Group of Newspapers was floated with £625 million value attaching to newspaper titles in the balance sheet. The titles made up the bulk of the shareholders' funds shown at £840 million. The valuation of the titles was undertaken by Coopers & Lybrand who also audited the accounts and reported on the flotation prospectus. The same firm had been auditing Maxwell businesses and pension funds for the last twenty years without ever issuing a qualified audit opinion.

In December 2001, Enron, a US based energy conglomerate, became the world's biggest bankruptcy. The company boasted annual revenues of some \$100 billion. The company's shares trading at \$90 each became worthless almost overnight. In November 2001, Enron's audited balance sheet boasted assets of some \$62 billion, but as investigations into alleged frauds were launched the company claimed that the assets were probably worth only \$38 billion (The New York Times, 23 April 2002). In its bankruptcy filing the company claimed that its audited financial statements from 1997 onwards should not be relied upon because of doubts about their accuracy. In the year 2000, Enron auditors Arthur Andersen received \$52 million in fees for services, comprising \$25 million for audit and \$27 million for consultancy services. Andersen's partners were incentivized to sell consultancy services to Enron. Their financial rewards were directly connected to these sales. The firm could not afford to upset Enron's directors and jeopardise its lucrative income stream. In 1999, Carl Bass, an Andersen partner, objected to Enron's accounting and off balance sheet financing schemes. This was not well received by Enron's directors. Bass was promptly removed from his job of providing oversight and approval of accounting issues to Andersen's audit team. The independence of Andersen's audits was also highly questionable because former Andersen professionals occupied over 300 middle and senior management positions at Enron. In many cases, the one-time audit

juniors were being asked to audit their former bosses. The alumni links enabled Andersen to sell internal auditing services to Enron, making Andersen part of the internal controls and management of the audit client.

The circumstances of Enron are not unique. In 1999, the Securities and Exchange Commission (SEC) charged Arthur Andersen with issuing "materially false and misleading audit reports on Waste Management" (press release, 19 June 2001). Andersen had been auditing Waste Management since its incorporation in 1971 and developed numerous relationships with the company and its executives. Until 1997, every chief financial officer and chief accounting officer was a former Andersen auditor. During the 1990s, approximately 14 former Andersen auditors worked for Waste Management, most often in key financial positions. Andersen sold numerous consultancy services to the company, including developing a strategic business model. Between 1991 and 1997, Andersen received \$7.5 million in audit fees and \$17.8 million in consultancy fees. In setting the compensation package of the partner responsible for the audit of Waste Management, Andersen took into account, among other things, the firm's billing to the company for audit and non-audit services.

In 1993, Andersen became aware of accounting irregularities of \$128 million (some 12% of the company's net income) at Waste Management. Rather than issuing a qualified audit report or requiring the management to immediately correct the errors, the audit firm agreed that the corrections should take place over the next five-to-seven years. Andersen also allowed the management to "bury" certain charges by improperly netting them against unrelated one-time gains. Ultimately, when the misstatements were revealed, Waste Management announced the largest income restatement in American corporate history. In issuing an unqualified audit report on the restated financial statements, Andersen acknowledged that the financial statements it had originally audited were materially misstated (SEC press release, 19 June 2001).

The issue of conflict of interests is again raised by the case of BCCI, a fraud infested bank that had been forcibly closed down (US Senate Committee on Foreign Relations, 1992). Price Waterhouse simultaneously acted as auditor, the eyes and ears of the regulators and advisers to BCCI management. BCCI hired the Consultancy Division of its auditors, Price Waterhouse(UK), to tackle losses from its treasury operations. The consultants completed their work in 1986 and the auditors [Price Waterhouse] reported that they were satisfied and that their recommendations for improving Treasury controls had been implemented. As a result of its review of the Treasury operations in 1985, the auditors also discovered a potential tax liability to the UK government, and subsequently

advised BCCI to move its Treasury operations out of the United Kingdom to avoid payment (Arnold and Sikka, 2001). In Price Waterhouse's words,

“In our report dated 28 April 1986, we referred to the control weaknesses which existed in respect of the group's Central Treasury Division (“Treasury”). During 1986 management engaged the services of the Consultancy Division of Price Waterhouse, London, to assist them in implementing recommendations contained in our earlier report. We reviewed the progress made by the bank on the implementation of revised procedures during the year and in a report dated 5 August 1986 we were able to conclude that most of our significant recommendations had been implemented. A further feature arising from the review of Treasury operations in 1985 was the potential liability to UK Corporation Tax arising from the Division's activities in the period 1982 to 1985. Following advice from ourselves and from the Tax Counsel during 1986 it was determined that this liability could be significantly reduced if the Bank ceased trading in the United Kingdom and claimed a terminal loss”.

Source: United States Senate Committee on Foreign Relations, 1992b, p.175.

BCCI's Treasury was moved from London to Abu Dhabi in 1986, Price Waterhouse assisting with the transfer. The audit firm acted as private consultants and advisors to BCCI management to further their 'private' interests. Yet at the same time the state was expecting them to perform 'public interest' functions by acting as an external monitor and quasi-regulator⁵. After the closure of BCCI (in July 1991), investigations into BCCI's criminality have been hampered by the fact some crucial documents had been transferred from London to Abu Dhabi.

The relationship between the management of BCCI and its auditors was so close that the US Senate concluded that "there can be no question that the auditing process failed to work" (US Senate Committee on Foreign Relations, 1992, p. 253). The US Senate report also found that

⁵ The Banking Act of 1987 required regular meetings between bank management, auditors and the Bank of England to discuss matters of mutual interest.

“BCCI provided loans and financial benefits to some of its auditors, whose acceptance of these benefits creates an appearance of impropriety, based on the possibility that such benefits could in theory affect the independent judgment of the auditors involved. These benefits included loans to two Price Waterhouse partnerships in the Caribbean. In addition, there are serious questions concerning the acceptance of payments and possibly housing from BCCI or its affiliates by Price Waterhouse partners in the Grand Caymans, and possible sexual favors provided by BCCI officials to certain persons affiliated with the firm.”

Source: United States Senate Committee on Foreign Relations, 1992b, pp. 4-5.

The UK government has failed to mount any independent investigation of the audit failures at BCCI. The typical response to any revelations conflicts of interests is to call for more professional pronouncements and ethical rules rather than set statutory rules, more public accountability and independent enforcement mechanisms. However, in pursuit of profits, accountancy firms are rarely constrained by codes of conduct or ethical statements issued by the accountancy trade associations (Mitchell et al., 1994). Money is far too important to them.

The DTI inspectors' report on Aveley Laboratories Limited (DTI, 1981b) noted that in pursuit of fees, the audit firm showed no regard to the ethical guidelines issued by the accountancy trade associations. Auditors were criticised for conflicts of interests arising out of the acceptance of the office of the receiver for their former clients. Conflicts of interests arising from financial relationships with the company and its directors also drew critical comments from the DTI inspectors' report on Scotia Investments Limited (DTI, 1981c). Yet the issues were to be repeated again.

Coopers & Lybrand (now part of PricewaterhouseCoopers) violated the so-called 'ethical' rules to secure the lucrative administration, receivership and liquidation of Polly Peck, a company with whom they had previous and on-going links (Mitchell et al., 1994). The ethical guidelines of the profession stated that firms should not accept such a position where "there is a continuing professional relationship" with the client. In accepting the position of the administrator, Coopers did not reveal its prior relationship with Polly Peck and its Chairman. The firm had acted as joint reporting accountants when Polly Peck originally went public. It had consultancy links with the company; advised the company chairman; played a role in the appointment of the company's finance directors and audited Polly Peck's Far East operations. After two years of public ridicule, the ICAEW found the partners guilty of violating the guidelines. The punishment for the guilty partners was a fine of £1000 (maximum possible). The firm is estimated to have made around £30

million from its insolvency appointment.

In pursuit of profits, accountancy firms continue to have deep organisational and cultural problems in complying with the rules. Further support for this view is provided by an investigation by the Securities and Exchange Commission (SEC). In June 2000, the SEC started a “look back” program and required major accounting firms to review their independence procedures and violations (SEC press release, 7 June 2000). As part of this, KPMG was admonished (SEC press release, 14 January 2002). The findings showed that contrary to the ‘independence’ rules, KPMG had a substantial investment in Short-Term Investment Trust (STIT), part of the AIM Funds, a collection of mutual funds audited by the firm. After the initial investment of \$25 million, KPMG made eleven additional investments and by September 2000, its investment constituted some 15% of the STIT’s net assets. The audit firm issued reports stating that it was “not aware of any relationships between [KPMG] and the [AIM] Funds that, in our professional judgment, may reasonably be thought to bear on our independence”.

The violation of the auditor independence rules was highlighted by third parties, as KPMG did not have the necessary organisational procedures. As the SEC put it,

“KPMG lacked adequate policies and procedures designed to prevent and detect independence problems caused by investment of the firm’s surplus cash. The failure constituted an extreme departure from the standards of ordinary care, and resulted in violations of the auditor independence requirements imposed by the Commission’s rules”.

Source: SEC press release, 14 January 2002, p. 6).

In January 1999, the US regulator, the SEC, censured PricewaterhouseCoopers (PwC) for “violating auditor independence rules and improper professional conduct” (SEC press release, 6 January 2000) and ordered an internal review of PwC’s compliance with the rules of auditor independence. As part of the review, PwC staff and partners were asked to self-report independence violations, and the independent reviewers were asked to randomly test a sample of the responses for completeness and accuracy. The review revealed more than 8,000 violations, including those from partners responsible for overseeing and preventing violations. The report concluded that there was

“widespread Independence non-compliance at PwC. despite clear warnings that the SEC was overseeing 77.5% of partners and 8.5% non-partners selected for audit in the Random Sample Study failed to report at least one violation. ... Many of the partners had substantial number of previously unreported violations. A total of approximately 86.5% of partners and 10.5% of non-partners in the Random Sample Study had at least one reported or unreported Independence violation. These results suggest that a far greater percentage of individuals in PwC’s firmwide population had Independence violations than was revealed by the self-reporting process The number of violations reflect *serious structural and cultural problems* [emphasis added] that were rooted in both its legacy firms [Price Waterhouse and Coopers & Lybrand merged to form PwC].”

Source: Securities and Exchange Commission, 2000, pp. 122-123.

In May 2002, the SEC accused Ernst & Young of violating the ethics rules by having a seven-year business relationship with a client, PeopleSoft (The New York Times, 21 May 2002). The SEC alleges that whilst Ernst & Young was auditing the company, its tax department and PeopleSoft jointly developed and marketed a computer program to help clients manage payroll and tax withholding for overseas employees. As part of the joint venture, Ernst & Young agreed to pay PeopleSoft royalties of 15% to 30% for each sale of the program.

In November 1995, Mitsubishi reported that it had caught Coopers and Lybrand altering work papers after the fact from an audit of Value Rent-A-Car, a company it just purchased. Value Rent-A-Car's audited financial statements showed a negative \$5.9 million net worth; in truth, the net worth was negative \$10 million. Coopers & Lybrand doesn't deny the revisionism, but called the changes "inconsequential." A Mitsubishi spokesperson said, "If we'd only seen the changed work papers first, we might never have purchased Value." (<http://multinationalmonitor.org/hyper/mm1295.04.html>, December 1995)

In principle, there is a possibility that the power of the accountancy firms may be checked by an investigation of their files and organisational values. However, as the next part shows, the affairs of accountancy firms are organised in such a way that they obstruct investigations.

Summary and Discussion

Instead of calling accountancy firms to account, the UK audit regulators are devoted to cover-up and obfuscation. Plenty of evidence exists to show that auditor independence is compromised by the sale of non-auditing services to audit clients, but the regulators pretend that no evidence exists. The Enron scandal has shown that major firms care little about the welfare of stakeholders. Audited company financial statements are hardly trusted by anyone. Many would like to see auditors act exclusively as 'auditors' and curb their collusive relationships with company management. However, the major accountancy firms see such changes as threats to their lucrative consultancy income streams. They have given the ICAEW, an audit regulator, £40,000 to mount public relations campaigns and preserve their fiefdoms. They have no regard for the social costs of audit failures that are borne by ordinary people.

The secrecy enjoyed by accountancy firms ensures that their collusive relationship with management remains hidden. They only come to light as the stench of scandals becomes overpowering. The auditing industry and the accountancy trade associations mediate the crisis by tweaking ethical guidelines and reinventing self-regulation. Such manoeuvres deflect attention from the structural and cultural problems at accountancy firms. The success of auditing firms is measured by increases in profits and fees. Their partners are rewarded for increasing the sale of consultancy services to audit clients. In pursuit of money, accountancy firms have shown no regard for ethical guidelines. The public has no way of checking compliance with such rules. The ethical guidelines encourage unethical conduct and have never required the firms to owe a 'duty of care' to audit stakeholders or publish any meaningful information about their affairs. In the absence of independent scrutiny, firms freely flout the rules.

CHAPTER 6

THE GLOBAL UNACCOUNTABILITY

Increasingly, accountancy firms secure audits of major corporations by claiming that they are 'global' organisations (US Senate Committee on Foreign Relations, 1992). With the aid of private sector organisations, such as the International Accounting Standards Board (IASB) and the International Auditing Practices Committee (IAPC), the firms have sought to develop standards and pronouncements that reduce their training costs, dilute liabilities and hence increase profits. The same vigour is missing in developing organisational structures that would enhance accountability or require accountancy firms to co-operate with local/global regulators. Four examples illustrate the arguments. These relate to real/alleged audit failures at Bank of Credit and Commerce International (BCCI), Enron, Barings and International Signal and Control Group.

In July 1991, amidst allegations of fraud, the Bank of England closed down the Bank of Credit & Commerce International (BCCI), considered to be the "world's biggest fraud" (Killick, 1998, p. 151). At the time of its closure, BCCI operated from 73 countries and had some 1.4 million depositors. Whilst there has been no independent investigation of the real/alleged audit failures in the UK, an inquiry by the US Senate concluded that "Regardless of the BCCI's attempts to hide its frauds from its outside auditors, there were numerous warning bells visible to the auditors from the early years of the bank's activities, and BCCI's auditors could have and should have done more to respond to them. The certification by BCCI's auditors that its picture of BCCI's books were "true and fair" from December 31, 1987 forward, had the consequence of assisting BCCI in misleading depositors, regulators, investigators, and other financial institutions as to BCCI's true financial position"⁶ (US Senate Committee on Foreign Relations, 1992, p. 4).

An examination of the working papers and files of the BCCI's auditors, Price Waterhouse (PW), had a considerable potential to provide public information about the organisational practices of auditing firms. It could also have provided some pointers for possible reforms. The US Senate sought access to auditor files. Despite claiming to be a 'global firm' Price Waterhouse remained reluctant to co-operate with international regulators. An investigation of BCCI by New York state banking authorities was also frustrated by the auditors' lack of co-operation. The New York District Attorney told the Congress that

⁶ It may be argued that auditors did not wish to qualify the accounts of a bank, for fear of causing a run. However, in 1999, PricewaterhouseCoopers issued a qualified report on the 1997-98 accounts of the Meghraj Bank, a major Asian bank with branches in the UK (Financial Times, 19 May 1999, p. 23)

“The main audit of BCCI was done by Price Waterhouse UK. They are not permitted, under English law, to disclose, at least they say that, to disclose the results of that audit, without authorization from the Bank of England. The Bank of England, so far -- and we’ve met with them here and over there -- have not given that permission.

The audit of BCCI, financial statement, profit and loss balance sheet that was filed in the State of New York was certified by Price Waterhouse Luxembourg. When we asked Price Waterhouse US for the records to support that, they said, oh, we don’t have those, that’s Price Waterhouse UK.

We said, can you get them for us? They said, oh, no that’s a separate entity owned by Price Waterhouse Worldwide, based in Bermuda”.

Source: United States Senate Committee on Foreign Relations, 1992b, p. 245.

BCCI’s auditors also refused to co-operate with the US Senate Subcommittee’s investigation⁷ of the bank (US Senate Committee on Foreign Relations, 1992, p. 256). Although the BCCI audit was secured by arguing that Price Waterhouse was a globally integrated firm (p. 258), in the face of a critical inquiry, the claims of global integration dissolved. Price Waterhouse (US) denied any knowledge of, or responsibility, for the BCCI audit which it claimed was the responsibility of Price Waterhouse (UK). Price Waterhouse (UK) refused to comply with US Senate subpoenas for sight of its working papers and declined to testify before the Senate Subcommittee on the grounds that the audit records were protected by British banking laws, and that “the British partnership of Price Waterhouse did not do business in the United States and could not be reached by subpoena” (p. 256).

PwC website refers to the firm as a “global practice”, but in a letter dated 17 October, Price Waterhouse (US) explained that the firm’s international practice rested upon loose agreements among separate and autonomous firms subject only to the local laws:

⁷ Price Waterhouse (UK) partners did agree to be interviewed by Subcommittee staff in PW’s London office. The offer was declined due to concerns that the interviews would be of little use in the absence of subpoenaed documents (US Senate, 1992, p. 258).

“The 26 Price Waterhouse firms practice, directly or through affiliated Price Waterhouse firms, in more than 90 countries throughout the world. Price Waterhouse firms are separate and independent legal entities whose activities are subject to the laws and professional obligations of the country in which they practice

...

No partner of PW-US is a partner of the Price Waterhouse firm in the United Kingdom; each firm elects its own senior partners; neither firm controls the other; each firm separately determines to hire and terminate its own professional and administrative staff.... each firm has its own clients; the firms do not share in each other's revenues or assets; and each separately maintains possession, custody and control over its own books and records, including work papers. The same independent and autonomous relationship exists between PW-US and the Price Waterhouse firms with practices in Luxembourg and Grand Cayman”.

Source: United States Senate Committee on Foreign Relations, 1992b, p. 257.

In December 2001, Enron, an energy conglomerate, became the world's biggest bankruptcy. Arthur Andersen, a worldwide accountancy firm, not only audited Enron's global business, but also provided numerous consultancy services, including internal auditing, tax and devising financial schemes. Andersen-Brazil rendered services for the Cuiaba, Brazil Power Plant. Andersen-India provided services related to the power plant in Dabhol. Andersen-UK provided services relating to commodities trading and the Wessex Water Company. Andersen cemented its close links with Enron by portraying itself as a global firm. As the events leading to Enron's bankruptcy unfolded Andersen allegedly engaged in a worldwide campaign to destroy any documents that could implicate it in the Enron frauds. In March 2002, a federal grand jury indicted Andersen on charges that Andersen knowingly persuaded employees in Houston, Chicago, Portland and London to withhold records from regulatory and criminal proceedings and alter, destroy and shred tons of documents with the intent to impede an investigation. A federal jury convicted Andersen on 15th June 2002. The 'global' credentials of accountancy firms once again came under scrutiny. Andersen website claims that the firms trading as Andersen trade under a “common brand, philosophy, technologies and practice methods [and have a worldwide] Board of Partners”, but in response to lawsuits and requests for documents, the firm claims that Arthur Andersen is not global. An official statement said that

"Arthur Andersen LLP [the US firm], an autonomous member firm of the Andersen Worldwide SC organisation, contracted with, performed the audits of, and signed the audit opinions on Enron's financial statements. Accordingly, Arthur Andersen LLP is the only proper defendant in claims relating to that audit opinion". John Ormerod, managing partner of Andersen in the UK, said: "Naming our firm as a defendant has no legal basis. While we have sympathy for those affected by Enron's failure, Andersen in the UK has no obligation to satisfy the legal liabilities of other member firms."

Source: <http://www.accountingweb.co.uk>; 9 April 2002.

The third example is Barings. On 26th February 1995, amidst revelations of £827 million fraud, Barings Plc collapsed (Bank of England, 1995). For many years prior to the collapse, Barings had been audited by Coopers & Lybrand (C&L). The Singapore office of C&L was appointed to audit the affairs of Baring Futures (Singapore) Pte Limited (BFS) for the year to 31st December 1994. The 1992 and 1993 accounts of BFS were audited by the Singapore office of Deloitte & Touche (D&T) who reported to C&L London for the purposes of its audit of the consolidated financial statements of Barings plc. C&L audited all other subsidiaries of Barings in 1992, 1993 and 1994 either through its London office or other offices spread around the world. As part of its inquiry, the Bank of England (BoE) sought access to the auditor files but the audit firms did not co-operate. The BoE noted,

"We have not been permitted access to C&L Singapore's work papers relating to the 1994 audit of BFS [Baring Futures (Singapore) Pte Limited] or had the opportunity to interview their personnel. C&L Singapore has declined our request for access, stating that its obligation to respect its client confidentiality prevents it assisting us".

"We have not been permitted either access to the working papers of D&T or the opportunity to interview any of their personnel who performed the audit. We do not know what records and explanations were provided by BFS personnel to them".

Sources: Bank of England, 1995, pp. 15 and 153.

The organisational structures and practices of accountancy firms also came under scrutiny in the aftermath of the financial problems at Ferranti, caused by the US\$1 billion fraud at one of its subsidiaries, International Signal and Control

Group Plc (ISC). The company was primarily engaged in the design and manufacture of military equipment. In 1987, the ISC and its subsidiaries, including a company called Technologies, were acquired by Ferranti. Technologies had factories and head office in the US and was audited by Peat Marwick Mitchell (PMM), subsequently part of KPMG. Over a period of time, \$1 billion worth of fraudulent contracts had been placed on ISC's balance sheet. Some directors of ISC had been engaged in a massive fraud and money laundering operation through shell companies in Panama, Switzerland and the US. The company's directors allegedly laundered \$700 million through the network of Swiss and US bank accounts. Fictitious contracts and transactions were created through offshore companies to boost profits. Following an investigation in 1988, ISC's founder and director pleaded guilty and was given a prison sentence. Ferranti bought the company without any knowledge of the frauds and sued auditors for negligence. An out of court settlement of £40 million was reached.

In response to complaints, the Joint Disciplinary Scheme (JDS), an organisation operating on behalf of the UK accountancy trade associations, was asked to investigate the matter. It sought sight of the audit working papers for the period 1986 to 1989. Its report noted that

“It quickly became clear that a substantial part of the audit work for Technologies had been undertaken on behalf of PMM in London by the American firm of the same name. considerable difficulties were experienced in gaining such access. ... I was informed that it was not that firms' policy to make papers available in situations of this kind. Copies of the American firm's working papers were eventually made available, “exceptionally and in order to assist the investigation”, at the offices of a law firm in New York. The copy files produced in New York were inadequate for the purposes of the investigation and it was necessary to arrange access to be gained to the original files. I was told that these were in the possession of the US Attorney in Philadelphia. My investigating accountants went there to examine them. They discovered that many of the files relevant for my purpose had remained in the possession of PMM. The firm had considerable difficulty in locating these files. Once they had been found a third visit to America was arranged. My investigating accountants were not permitted to photocopy relevant material of an any of American firm's files, rendering extensive note-taking necessary.”

Source: Joint Disciplinary Scheme, 1996, p. 7.

Summary and Discussion

The structure of major accountancy firms has been carefully organised to maximise their profits and minimise accountability. Major accountancy firms use the same name, logo and stationery and advertise themselves as ‘global’ organisations. They claim to have the ‘global’ structures and organisation to audit businesses and sell integrated consultancy services. The firms secure business by parading their ‘global’ credentials. Their partners share revenues generated by global clients.

Episodes such as Enron, BCCI, Barings and other episodes show that when the firms are called to account, their charade of being ‘global’ dissolves away. At critical times, major firms claim that they are no more than a disparate collection of ‘national’ firms or franchised businesses. As the Manhattan district Attorney put it, “Even McDonald’s has more control over its franchises” (New York Daily News, 10 January, 1999).

The ownership structure of major accountancy firms is complex and secretive. Most seem to be ultimately owned by trusts registered in secretive offshore tax havens with no information sharing treaties with major nations. Such structures have been carefully developed to shield accountancy firms from public scrutiny and liability for their failures. The ultimate losers are the stakeholders affected by the failures of accountancy firms.

The auditing regulators are aware of the culture of non-co-operation, but are reluctant to scrutinise the practices and policies that give rise to it. They could punish firms that refuse to co-operate with named international regulators. The government could introduce legislation requiring all Plc auditors to co-operate with named regulators. If the firms refuse, the DTI and the audit regulators could step in and cancel the firm’s licence to sell audits. But accountability of the auditing industry has been organised off the political agenda. So audit failures are not fully investigated and firms avoid accountability. Through these structures, the firms also avoid co-operation with the regulators tracking down ant-social activities (see chapter 3).

CHAPTER 7

SHIELDING THE AUDITING INDUSTRY

Auditing is in urgent need of reform. But the accountancy establishment does not want meaningful change. It is only concerned about its profits and fees. It wants to use audit as a market stall to sell consultancy services. It does not want independent regulation, or to owe a 'duty of care' to the individuals injured by its practices. It does not wish to publish information about its affairs, co-operate with international regulators or curb any of its anti-social activities. So with the help of the Department of Trade and Industry (DTI) it has organised its accountability off the political agenda.

Accountancy industry has used its financial and political resources (including hiring MPs) to advance its narrow economic interests. Former Conservative MPs Tim Smith and Jeremy Hanley were on the books of the ICAEW and accountancy firms, most notably Price Waterhouse. They used their position to defend self-regulation and the economic privileges of the auditing industry. Labour MPs Stuart Bell and Peter Mandelson acted as consultants for Ernst & Young. Stuart Bell played a major role in securing Limited Liability Partnerships (LLPs) and diluting audit firm liability. Within days of failing to secure a post in the 1997 Labour government he became a consultant to Ernst & Young. Upon becoming Secretary of Trade & Industry, Peter Mandelson scuppered the possibility of independent regulation for the accountancy industry. Within days of leaving office in controversial circumstances, he too became a consultant to Ernst & Young. Major firms also donate monies and services to political parties to secure favourable policy outcomes. None of this encourages regulators to curtail their dirty business or do anything to check their abuses. These have caused loss of homes, jobs, savings, pensions, investments and tax revenues (see Mitchell et al., 1991; Sikka and Willmott, 1995a, 1995b; Sikka, 2001).

The auditing industry always blames others for its own failures. It is the fault of company directors, poor accounting rules, unrealistic public expectations, or something else. If that does not work then ethical rules and disciplinary arrangements are tweaked, soothing reports are issued and another ineffective self-regulator is wheeled out. All the time, the auditing industry is shielded from scrutiny. Little or nothing has been done to make auditing firms accountable to the public, or examine the organisational culture of accountancy firms. This strategy has been applied during the 1970s, the 1980s, the 1990s and beyond.

In the late 1960s, industrialists such as Lord Kearton raised concerns about poor

auditing practices (Robson, 1991). Such concerns were emphasised by scandals at Rolls Razor and the pliability of accounting numbers during the controversial GEC/AEI merger. The public concern was about the poverty of auditing practices, but with the aid of the DTI the accountancy establishment reconstructed the issues as problems of accounting. As a result, the Accounting Standards Steering Committee (ASSC), subsequently the Accounting Standards Committee (ASC), was born in 1970. The accounting standard setting machinery was mostly under the control of accountancy firms. The accountancy establishment also published a soothing report which held out the promise of reforms in the near future (Accounting Standards Steering Committee, 1975).

The poverty of auditing practices again hit the headlines. The scandals at London & Counties, London and Capital, Stern Property Group, Vehicle and General, Court Line, Scotia Investments, Grays Building Society, Moorgate Mercantile, Cedar Holdings, and the related secondary banking, property, shipping and insurance crash, once again highlighted the poverty of auditing practices. The British taxpayer bailed out the ailing banking and property sectors by handing out £3,000 million. The government had to ask the International Monetary Fund (IMF) for help. Under external pressure, the Auditing Practices Committee (APC) was formed to promulgate auditing standards, all under the control of major accountancy firms, the very firms whose standards had brought about audit failures (Sikka, Willmott and Lowe, 1989). Its mission was "to satisfy our critics in political circles and outside" (APC, 1978, p. 50) and to "assist the auditing profession in defending itself against unnecessary and inappropriate claims" (APC, 1986, p. 61). The APC excluded the public from all its meetings and did not owe a 'duty of care' to anyone. It urged auditors to be 'passive' (Sikka, 1992) and sought to defend the auditing industry by restricting its responsibilities.

A formal programme of ethical guidelines also began in the 1970s. They did not require auditors to publish any meaningful information or urged them to owe a 'duty of care' to anyone. Auditors were not urged to act exclusively as auditors. Rather than making negligent accountancy firms subject to public hearings or independent inquiries, the DTI gave them their own 'private' investigation system. The Joint Disciplinary Scheme (JDS) was formed with a view to investigating major audit failures. Much of the financial support came from the largest auditing firms (The Accounting Bulletin, March 1983, p. 9) - the very firms that had been criticised in the DTI reports. Their partners sat on most subsequent inquiry panels, acting as judges and juries, carefully ensuring that the benchmarks were low enough and could not come back to haunt them. With the approval of the DTI, it was agreed that firms could not be fined more than £1,000, no matter how negligent they were.

By the 1980s, more auditing failures emerged as Johnson Matthey, De Lorean, Sound Diffusion and other companies collapsed. Despite the earlier promises, no fundamental reform of the auditing industry took place. Following the adoption of the EU Eighth Directive, the UK government published its proposals for the regulation of auditors (DTI, 1986). The document raised the prospect of an independent body to regulate auditors. But the government gave in to lobbying by accountancy firms and accountancy trade became formal regulators (under the Companies Act 1989) of the auditing industry. The ICAEW released its report on the future of the audit (ICAEW, 1986). It promised major reform of auditing, but nothing happened.

The late 1980s and the early 1990s brought more audit failures to public attention. Businesses such as Maxwell, British and Commonwealth, Polly Peck, Levitt Group, Coloroll, Barlow Clowes, Dunsdale, Air Europe, Maxwell, BCCI, International Signal and Control (ISC) and Sock Shop collapsed within a short time of receiving unqualified audit opinions. Once again, the crisis was mediated by blaming accounting practices. In 1990, the ASC was turned into the Accounting Standards Board (ASB). Its present chairperson is a partner from PricewaterhouseCoopers. In 1991, the APC was turned into the Auditing Practices Board (APB). Its present chairperson is a partner from Arthur Andersen. There was the usual promise to tweak the ethical guidelines and toughen the disciplinary arrangements, but no attempt to explain previous failures. The DTI helped the industry by ensuring that there would be no independent investigation of audit failures at Levitt, BCCI and Polly Peck.

The well-tried and trusted tactic of promising reforms was used again. In cooperation with the Confederation of British Industry (CBI) and the London Stock Exchange, the ICAEW set-up a Committee to examine corporate governance under the chairmanship of Sir Adrian Cadbury. The report (Committee on the Financial Aspects of Corporate Governance, 1992) sought to preserve self-regulation. It supported the status-quo and opposed any ban on the sale of non-audit services, or reform of auditor duty to stakeholders. It advocated more fee earning opportunities by recommending that accountancy firms report on interim accounts and internal controls. A similar pattern is followed by the Hampel Report on corporate governance (Committee on Corporate Governance, 1998).

The incoming Labour government of 1997 could find no legislative time to reverse the 1990 *Caparo* judgement, nevertheless it enacted the Limited Liability Partnership (LLP) Act 2000. This shielded accountancy firm partners and reduced the legal redress available to the innocent victims of malpractices by accountancy

firms. The chief architect of this policy was the 1997 Labour Trade and Industry spokesperson Stuart Bell MP. Labour also lifted the previous government's ban on Arthur Andersen, imposed after the De Lorean debacle, to enable it to secure government consultancy contracts. Rather than scrutinising the organisational culture of accountancy firms, the government used them to advance its Private Finance Initiative (PFI) and the Private Public Partnership (PPP) policies for privatising vast swathes of the public sector. The DTI ensured that there would be no independent investigation of audit failures at Resort hotels, Equitable Life, Independent Insurance and other debacles. Instead of keeping to its previous Labour promises of ending self-regulation, Peter Mandelson, Secretary of State for Trade & Industry, rejected independent regulation of the auditing industry and created five more regulatory bodies under the umbrella of the Accountancy Foundation. Now accountancy business is regulated by 23 regulators (see Appendix 1), but the system does not have an independent complaints investigation system or an ombudsman to adjudicate on complaints.

The usual trick of soothing reports, tweaking ethical guidelines and disciplinary arrangements is once again in operation. The Ethics Standards Board (ESB), one of the offshoots of the Accountancy Foundation, has issued proposals (in May 2002) for revising the ethical guidelines. Its proposals do not urge accountancy firms to accept a 'duty of care' to any individual stakeholder or a requirement to make firms publicly accountable. New disciplinary arrangements are also being mooted. No one has explained why it took the JDS 10 years to deal with the Maxwell debacle, or why Coopers & Lybrand were fined only £1,000 for violating the ethical rules and accepting the lucrative Polly Peck receivership.

Some Reflections

Auditing is regulated through a variety of formal and informal processes, including the education and training of accountants, the legal environment and the formal regulatory arrangements, often involving the state and accountancy trade associations. However, little attention is directed at the capacity of organisational cultures of accountancy firms to facilitate damage to a wide variety of people.

One might expect accountancy education to become a catalyst for reform. In fact, it is under the control of accountancy trade associations. Most of the auditing education, especially professional education, is primarily technical in nature. Considerable attention is paid to learning the official auditing standards and other pronouncements without any study of the practical politics of auditing. Such studies show that auditing standards are often driven by the auditing industry's

concerns to minimise its responsibility and liability (Sikka, 1992). They rarely pay any attention to the organisational practices of accountancy firms, or open them up to public scrutiny. Auditing education rarely focuses upon the theories underpinning auditing knowledge, far less consider its limitations and failures (Sikka, 1987; Puxty et al., 1994). Almost every week, newspapers highlight new audit failures. Yet students are taught knowledge that has already explicitly failed. No questions are raised about the domination of auditing standard setting by the auditing industry, its patrons, its values and business interests. The consequences of auditing knowledge and practices could be analysed by discussing audit failures, but such matters rarely form part of auditing education. There is rarely any discussion of the relationships, tensions and consequences arising out of the auditing arrangements that expect business organisations (accountancy firms) to perform social surveillance.

The law has the capacity to change the economic incentives for delivering poor audits. It is common practice to require producers of sweets and potato chips/crisps to owe a 'duty of care' to third parties, but the same does not apply to producers of audit opinions. The legal position, as summed up by the Law Lords in the case of *Caparo Industries plc v Dickman & Others [1990] 1 All ER HL 568* is that, generally, auditors only owe a 'duty of care' to the company, as a legal person. They do not owe a 'duty of care' to any individual shareholder, creditor, pension scheme member or any other stakeholder. The regulators (e.g. the accountancy bodies) routinely campaign to demand liability concessions for auditing firms (Cousins et al., 1998). They have failed to give any thought to the consequences of their campaigns for the institutionalisation of audit failures.

The overall responsibility for regulating the UK auditing industry rests with the Department of Trade and Industry (DTI). From time to time, it appoints inspectors to examine unexpected corporate collapses and frauds. As part of the inquiries, the inspectors may focus upon the conduct of company audits. However, some of the reports have been suppressed whilst others take many years to publish (Sikka and Willmott, 1995b; Department of Trade and Industry, 2001). The DTI does not have an adequately resourced in-house investigation unit. Instead, it appoints partners from major accountancy and law firms to act as inspectors. The inspectors rarely examine the impact of organisational culture and values on audit failures. By holding out the threat of punitive action, the DTI could create the economic incentives for accountancy firms to reflect upon the consequences of their anti-social practices. However, it has failed to prosecute any auditing firm or its partners for delivering poor audits. Nor has it mounted any investigation into the organisational culture of the firms implicated in dirty business.

Since the Companies Act 1989, the accountancy bodies have been acting as regulators of the UK auditing industry. As part of their regulatory obligations, they licence, monitor and discipline auditors and also investigate instances of real/alleged audit failures. As part of their monitoring duties, the regulatory bodies could specifically examine the impact of organisational practices upon audits, but they have not done so. Instead, they claim that "the main purpose of practice monitoring is to monitor compliance with auditing standards, rather than to obtain statistical information about the quality of work being done" (Page 25 of the ACCA's 1992 annual report on Audit Regulation) and that the "principal purpose of monitoring is to enable the ARC's [Audit Registration Committees] to satisfy themselves that registered auditors comply with the Audit Regulations" (Page 5 of the 1992 ICAEW, ICAS and ICAI annual report on Audit Regulation). The focus on mechanical compliance with auditing standards (which are not independently formulated) pays little attention to the organisational culture that facilitates audit failures.

Conscientious accountancy bodies would support calls for changes to the legal and institutional structures so that the accountancy firms are persuaded to revise their organisational structures and values. Instead, they routinely side with the producers/sellers of audits (Cousins et al., 1998; Mitchell et al., 1998) and consider themselves to be primarily "responsible for protecting and promoting the interests of [their] members" (Certified Accountant, September 1991, p. 12). They have a history of opposing any association of audits with detection and reporting of fraud (Sikka et al., 1998). Even in the aftermath of the BCCI scandal, the auditing industry opposed the imposition of any 'duty' to report financial irregularities in financial businesses (e.g. banks, insurance and financial services companies) to the regulators (Bingham, 1992). Historically, the accountancy bodies have opposed obligations for companies to publish the profit & loss account, balance sheet, market value of assets, group accounts, movements on reserves, audit reports, corporate turnover and the need for companies to have independent audit committees, just to mention a few (Puxty et al., 1994). The accountancy industry and its patrons rarely see the problems from the perspective of the wider public that might be affected by their policies.

CHAPTER 8

SUMMARY, DISCUSSION AND PROPOSALS FOR REFORM

Newspapers and government routinely draw attention to street crime, muggings and violence. Yet they totally ignore the dirty business of accountancy firms. In pursuit of profits, accountancy firms operate cartels, launder money, facilitate tax avoidance/evasion, bribery and obstruct inquiries into frauds and deliver shoddy audits. Equitable Life, Independent Insurance, Enron, Transtec, Wickes, Resort Hotels and Tyco are some of the recent additions to a long line of audit failures. Millions of innocent people have lost their jobs, savings, investments and pensions. The accountancy industry is shielded from the consequences of its own failures by poor liability laws and the Limited Liability Partnership (LLP) legislation. Rather than reflecting upon its organisational practices and irresponsibility, the accountancy industry is demanding even more liability concessions.

The requirement to increase fees and profits shapes the organisational practices and culture of accountancy firms. They standardise audits and exploit labour, expecting staff to work excessive hours for no/little pay. Some staff respond to such pressures by resorting to irregular auditing practices, unauthorised short-cuts and falsification of audit work. Despite the proliferation of auditing standards on planning, controlling, recording and review of audits (Auditing Practices Committee, 1980), the audit working papers are not necessarily reviewed by another partner/manager. Firms routinely destroy notes and files that might assist investigators (Department of Trade and Industry, 1995, p. 324-325). Despite laws strengthening the position of resigning auditors, accountancy firms seem to be keen to walk away quietly from troublesome situations. To advance their economic interests, audit firms enter into private deals with company directors, assuring them that they will obstruct inquiries and not easily provide meaningful information to stakeholders. Some accountancy firms have also devised organisational structures that thwart co-operation with the regulators. They are headquartered in offshore financial centres that are known for their secrecy and lack of co-operation with international investigators and regulators (Mitchell et al., 2002). Such structures and practices are the result of carefully nurtured policies and values, probably put in place after strategic discussions amongst partners and with legal advisers. The organisational practices seek to advance the short-term economic interest of auditing firms and provide the context for understanding audit failures.

In an environment that links performance to profits, bonuses, salaries and

promotion, accountancy firms (and their partners) are reluctant or unwilling to offend corporate sensitivities, as a reputation for being troublesome may not be conducive to securing auditing and lucrative consultancy business. Audit failures 'reveal shortcomings in both vigilance and diligence' and 'a failure to achieve an appropriate degree of objectivity and scepticism' (Joint Disciplinary Scheme, 1999). Rather than focusing attention upon the role of organisational cultures and practices in facilitating audit failures, the tendency of the auditing industry and its regulators is to deflect attention. The typical strategy has been to individualise audit failures (Sikka, 2001), blame company directors, corporate governance practices, lax accounting standards and the expectations of significant others (Sikka et al., 1998). This way, the organisational practices and values responsible for audit failures remain shielded from scrutiny and audit failures remain institutionalised.

Some questions about organisational practices could be raised by the availability of meaningful information. However, accountancy firms are some of the most secretive organisations in the world. Information about auditor relationships with companies, conflict of interests, details of the audit team, audit contract, audit effort, profitability and contents of auditor files is remarkably scarce. In principle, the imposition of stringent liability and 'due care' laws could persuade accountancy firms to reflect upon the consequences of their organisational practices. However, the legal environment is weak. Due to inequalities in wealth distribution and cuts in legal-aid, many injured stakeholders do not have the necessary financial, legal and political resources to challenge the firms and facilitate a public scrutiny of their organisational practices. The regulators could generate pressures for changes in cultures dominating accountancy firms, but they have a close and cosy relationship with auditing firms. The auditing industry is regulated by the accountancy trade associations who are also responsible for promoting and defending the industry. To be effective regulators also need economic pressures, but they do not owe a 'duty of care' to anyone relying upon their monitoring, licensing and disciplining activities.

The problems of auditing are the result of changes in capitalism, but no regulator is examining the shift in capitalist economies from industrial capitalism to finance capitalism where money itself has become a commodity. Due to technological developments, money easily roams the world. There is no longer any relationship between money, credit and the productive economy. Rather than directly investing in the production of goods and services, corporations make money by placing clever bets (gambling or hedging) on interest rate movements, exchange rates, security prices, commodities and land speculation. Not surprisingly, many of the major scandals and audit failures have occurred in the financial sector (BCCI, Savings &

Loan, Levitt, Barlow Clowes, Wallace Smith, Barings, Yamaichi). Yet this malaise is not restricted to just the financial sector. Companies in all sectors are pursuing get-rich quick schemes. Enron, primarily an energy company, had been heavily engaged in financial engineering. Major companies (Enron, BT, NTL, Vodaphone NewsCorp) are funding their growth by debt rather than equity. Enron was one of the world's largest traders in derivatives. The value of corporate debt (unlike bank loans) is not fixed and companies can conceal liabilities through all sorts of offshore vehicles. The changes call for extensive surveillance and regulation of corporations. But auditing firms themselves are also part of the problem. They sell financial engineering, front shell companies, devise complex corporate structures and other devices to enable their clients to massage the accounts and avoid accountability. They maximise their private profits by hiding behind the 'duty of confidentiality' to client and ignore any obligations to the public. This prioritising of 'private' interest over the 'public' interest has injured bank depositors, pension scheme members and other stakeholders. They sell 'consultancy audits' rather than 'independent audits' and their opinions are almost worthless.

The new economy requires reflections on accounting, auditing and regulation. Clearly new institutional arrangements are needed to end the dirty business of accountancy firms and check their power to do social damage. The reforms could include the performance of audits by the staff of the regulators. Taxation authorities (e.g. Inland Revenue, Customs & Excise) are already empowered to conduct independent audits of specific aspects of business. Their jurisdiction could be extended. The employees of the regulators (e.g. the Financial Services Agency) could conduct audits. Unlike the BCCI auditors, they would not easily be able to hide behind the veil of 'confidentiality', nor would they refuse to co-operate with other regulators, or act as consultants to the audit clients and acquire a vested business interest. Auditors frequently claim that the public does not understand the functions and purposes of an audit. Therefore, they can't have too many objections, if representatives of the public take over the external audit function.

As the auditing industry has "ditched any pretence of their being public spirited" (Hanlon, 1994, p. 150), its interests should be secondary to those concerned with the protection of stakeholders. The development of alternative policies can enrich public debates. It could be argued that external audit be made non-mandatory and replaced with new public policies. One could require all companies and their directors to have compulsory insurance (say some multiple of gross assets) so that adequate protection is available to stakeholders against fraud. The second policy would require the introduction of legislation that specifies (or authorises a regulatory body to specify) the kind of information companies must publish. Failure to publish the required information and maintain adequate insurance cover would be

a criminal offence which would make directors and officers personally liable for company's debts. As insurance premiums would be dependent upon some estimation of risk, insurance companies could ask accountancy firms to make appropriate investigations and report. In such circumstances, the insurance companies and the auditing firms would have to negotiate the terms on which corporate risks are to be assessed. Auditing firms would have to accept fraud detection/reporting as an objective of each assignment. Under such scenarios, the audit function (as we now understand it) would in practice be taken over by the insurance industry, but the public would have a real protection from fraud. Sadly, the government does not have the desire to think new policies.

If the current policies are to be pursued then, ideally, company directors should have no say in the appointment and remuneration of auditors. Audits of major companies should be carried out by a government department. Government should empower the National Audit Office, Inland Revenue and Customs & Excise to perform company audits. This might not only produce independent audits, but also increase the tax revenues, as auditors would be less willing to go along with doubtful practices. What is likely to worry company directors more? A visit from Inland Revenue or a visit from a Big Five/Four accountancy firm? However, we do not live in an ideal world. Governments are unlikely to have the backbone to support such proposals. Accountancy firms and their patrons would mobilise their economic and political resources to oppose anything that curbs their ability to mould financial statements.

Therefore, the government is likely to opt for the Nth best solutions. The solutions have to be appropriate for dealing with a powerful industry that routinely fails and harms innocent people. If audits are to be conducted by the private sector then reforms are essential.

- Instead of 23 separate regulators, a single statute-based independent regulator, namely a Companies Commission, should regulate accountancy business, taking over all the licensing and monitoring powers currently exercised by the accountancy trade associations.
- The Companies Commission should each year review the changes in the economy and consider the resulting changes needed in accounting and auditing.
- The Companies Commission shall take responsibility for selecting and appointing auditors for all quoted companies. Such appointments should be ratified by a simple vote of individual shareholders, employees and bank

depositors, where appropriate. Directors shall not be able to subvert this decision by proxy votes.

- If the company stakeholders are dissatisfied with the proposed audit firm they may nominate an alternative firm.
- The members of the Companies Commission should sever all connections with their employers so that, unlike their part-time counterparts in the current ASB and APB, they can speak openly on all issues without fear of sanctions by their paymasters. To minimise the chances of 'capture', members should serve for a maximum of five years. Accounting and auditing issues are essentially about wealth distribution, accountability, risk management, social justice and fairness. Therefore, the membership should reflect a wide constituency, with accountants, as technical experts, available in an advisory capacity. Regulatory structures and processes should not be dominated by the cloak of technical interests. The assumed technical experts should not be able to formulate social policies under the guise of 'techniques' to mystify others.
- The Commission should meet in the open and pursue a 'full sunshine' policy, with agenda papers and minutes accessible to any member of the public on payment of a modest fee. The composition and terms of reference of all working parties should be announced and the results of votes made publicly available.
- Public hearings should be an integral part of the accounting/auditing standard setting process. It should be an offence for two or more members of the regulatory body to meet in private and fix the contents of proposed regulations. Indeed, at the beginning of each meeting, members should clearly state that they have not violated this requirement.
- Unlike the present position, the regulator should owe a 'duty of care' to the parties affected by its decisions.
- The Companies Commission should consider ways of expanding the supply of auditors. For example, by authorising new organisations (e.g. Inland Revenue, National Audit Office, non-governmental organisations) to conduct company audits. This would also break the monopoly of the Big-Four.
- The Companies Commission should investigate incidences of audit failures and publish speedy reports.

- The Companies Commission should have a statutory right of access to all auditor working papers, with powers to investigate the overall standards and organisational practices of firms implicated in audit failures.
- The Companies Commission should have the right to pass copies of auditor working papers to recognised international regulators. Accountancy firms should not be able to obstruct (as in the case of Enron, BCCI, Barings, International Signal Corporation Group) international inquiries.
- The Commission shall have the powers to fine and prosecute firms and to secure undertakings from the firms, e.g. to improve their quality control and organisational practices. Those failing to deliver improvements should be closed down.
- To ensure that the public is protected, the Commission should list the names of the firms whose standards have been found to be inadequate during any monitoring visit.
- Complaints against the Commission should be investigated by an independent Ombudsman with periodic scrutiny from the Parliamentary Trade and Industry Select Committee.
- Auditors and stakeholders should be able to seek a judicial review of the recommendations of the Commission.
- Companies should have directly elected (e.g. by shareholders and employees) full-time non-executive directors. They should not hold shares in the company. They should not be able to hold directorships of more than one group of companies.
- Auditors should act exclusively as auditors. The state guaranteed market of external auditing was not given to accountants to enable them to use it as a foot-in-the-door to sell other services. Auditors should not be allowed to sell consultancy services to any audit client. Neither the audit firm nor any of its associates shall be a party of any part of the financial statements being audited. In reality, Auditors have become personnel departments and extensions of finance departments of the companies they audit. In Germany auditors are prohibited from selling consultancy services to audit clients. In the UK, the Audit Commission appoints local authority auditors. They are generally prohibited from selling consultancy services to the local authorities that they

audit. In the corporate sector, auditing firms devise tax avoidance schemes, off-balance sheet financing schemes, dream up creative accounting ideas, corporate strategy, write-up books, advise on mergers, acquisitions and factory closures. All this makes them as dependent as any other door to door salesman. It compromises their independence. The auditors are expected to act as referees and umpires, but their reliance on directors and their financial involvement with the companies give them little incentive to report unsavoury practices. They cannot be independent of the directors and have acquiesced to numerous novel accounting practices. As the accountancy trade associations frequently claim, 'the auditors not only needs to be, but must also be seen to be independent'.

- At every AGM there should be a declaration that the directors have not used the auditor or any of its associates for any non-auditing services.
- No auditor shall remain in office for a period exceeding five/seven years. The longevity of the auditor's term in office played a part in auditor silence at Maxwell, Levitt, Queens Moat Houses, Polly Peck, Grays Building Society and many other places. A fresh broom and eyes are highly desirable.
- Where the company's auditors have been changed during the year a report shall be filed with the Registrar of Companies stating the matters discussed by the directors with the proposed auditors. If any of the company's accounting policy changes coincide with the replacement of auditors they shall be explained and the auditors should state whether they have agreed to such changes. 'Opinion shopping' is a widespread phenomenon in the UK. Directors approach auditing firms and ask whether they approve of particular accounting policies, frequently designed to show company performance in the best possible light. Directors have economic incentives to go 'opinion shopping', as their salary, pensions, perks and bonuses are increasingly linked with accounting measures rather than market shares, innovations, quality of production, or consumer satisfaction. The legal fiction is that auditors are hired and fired by shareholders. The practical reality is that auditors are hired and fired by directors and they can be in close collusion even to the extent of devising tax, transfer pricing and other accounting dodges. For all practical purposes, directors are the 'clients' of auditors. Auditors depend upon directors for their continuation in office and in the face of competition from other firms, they are all too willing to push unacceptable practices. Public disclosure is a vital means of alerting the public.
- Auditor's duties should be specified by statute. The Companies Acts spell out the directors' duties in considerable detail. Similar detail is absent for auditor

responsibilities. The auditing industry is quite happy, for it prefers vague arrangements which enable it to dodge responsibilities and shield fee earning opportunities. The accountancy trade associations claim that auditors are not responsible for detecting and reporting fraud (after BCCI the financial sector auditors have a 'duty' to report irregularities to the regulators) or for commenting on business efficiency, effectiveness and financial soundness etc. Yet such audit objectives are commonplace in the public sector. Auditors of all PLCs should be required to report search and report any material fraud to the appropriate regulators.

- Auditor working papers should be available for inspection by designated representatives of stakeholders (e.g. a directly elected audit committee).
- No member of the audit team should obtain paid employment with an audit client for a period of five years since the last audit visit.
- Auditors shall owe a 'duty of care' to the individuals who are shareholders, creditors, pensions scheme members and employees at the date of the audit report.
- The incoming auditor should have a statutory right of access to the files and working papers of the outgoing auditors. This will enable them to make a better and informed assessment of the desirability of the client and also appreciate the validity, or otherwise, of the statements issued by the resigning auditor.
- Anyone authorised to conduct the audit of a public limited company should be required to publish meaningful information about their affairs. They should be required to file copies of the audit contract, audit tender, report on companies internal controls, composition of the audit team, relationship with company directors, related companies, assurance given/received from directors, conflicts of interests, details of meetings held with the audit committee, and so on.

If we are to transform the existing practices, the first step must be to create a framework which allows voices, so far stifled, to be heard. The opening up of structures can advance competing discourses and values, something that is essential if emancipatory change is to take place. A strengthened regulatory, legal and accountability environment would give auditors incentives to reflect upon their narrow pursuit of economic interests.

These suggestions are sure to be opposed by the accountancy industry which has a long history of opposing reform (Puxty et al, 1994, Bingham, 1992). Yet can that industry continue to hold the public to ransom and dissociate itself from the consequences of its own failures? Should it be allowed to? Successive governments have underwritten the power of major accountancy firms and given them state guaranteed markets and protection from liability. They have done little to check their dirty business, or protect the public from their anti-social practices. New Labour's strategy of co-operating with big business has encouraged major firms to become even more anti-social. They consider themselves to be immune from any inquiry or reform. The price of this indulgence, as the Enron scandal shows, is being paid by people losing their jobs, homes, savings, investments and pensions.

APPENDIX 1
Regulation of Accountancy Business

Regulation of Financial Reporting (4)

Financial Reporting council
Accounting Standards Board
Financial Reporting Review Panel
Urgent Issues Task Force

Regulators of Auditing (5)

The Institute of Chartered Accountants in England & Wales (ICAEW)
The Association of Chartered Certified Accountants (ACCA)
The Institute of Chartered Accountants of Scotland (ICAS)
The Institute of Chartered Accountants in Ireland (ICAI)
The Association of Authorised Public Accountants (AAPA)

Regulation of Insolvency (8)

Institute of Chartered Accountants in England & Wales (ICAEW)
Insolvency Practitioners Association (IPA)
Law Society of England & Wales
Institute of Chartered Accountants of Scotland (ICAS)
Association of Chartered Certified Accountants (ACCA)
Institute of Chartered Accountants in Ireland (ICAI)
Law Society of Scotland

Secretary of State for Trade and Industry

Regulation of Accountancy Profession (5)

Accountancy Foundation
The Review Board
Ethics Standards Board
Auditing Practices Board
Investigation and Discipline Board/Joint Disciplinary Scheme

For Investment and Financial Services (1)

Financial Services Authority

NOTE: There is some overlap. The above list would be even longer if the Joint Monitoring Unit (JMU) and Joint Insolvency Monitoring Unit (JIMU) were included. Both are registered as separate organisations, but are owned by the accountancy bodies. The above list also excludes the five Recognised Qualifying Bodies (RQBs), effectively the professional accountancy bodies, whose qualifications must be passed to enable anyone to become an auditor or an insolvency practitioner.

Bibliography

Accounting Standards Steering Committee, (1995). **The Corporate Report**, London, ASSC.

Altman, E.I., (1968). Financial Ratios, Discriminant Analysis and the Prediction of Corporate Bankruptcy, **Journal of Finance**, September, pp. 589-609.

Altman, E.I., and McGough, T.P., (1974). Evaluation of a company as a going concern, **Journal of Accountancy**, June, pp. 50-57.

Arnold, P., and Sikka, P., (2001). Globalization and the State-Profession Relationship: The case of the Bank of Credit and Commerce International, **Accounting, Organizations and Society**, Vol. 26, No. 4, pp. 475-499.

Auditing Practices Board, (1995a). **Statement of Auditing Standards 300: Accounting and internal control systems and audit risk assessment**, London, APB.

Auditing Practices Board, (1995b). **Statement of Auditing Standards 430: Audit Sampling**, London, APB.

Auditing Practices Board, (1995c). **Statement of Auditing Standards 410: Analytical Procedures**, London, APB.

Auditing Practices Committee, (1978). **True and Fair: Issue 7**, Spring, London, APC.

Auditing Practices Committee, (1980). **The auditor's operational standard**, London, APC.

Auditing Practices Committee, (1986). **APC: The First Ten Years**, London; APC

Bank of England, (1995). **Report of the Board of Banking Supervision Inquiry into the Circumstances of the Collapse of Barings**, London, HMSO.

Beck, U., (1992). **Risk Society: Towards a New Modernity**, London, Sage.

Bingham, The Right Honourable Lord Justice, (1992). **Inquiry into the Supervision of The Bank of Credit and Commerce International**, London:

HMSO.

Black, E., (2001). **IBM and the Holocaust**, London, Little Brown.

Chitty, D., (1999). No end of a lesson, **Accountancy**, May, p. 108-109.

Chomsky, N., (1999). **Profit over People: Neoliberalism and Global Order**, New York, Seven Stories Press.

Committee on the Financial aspects of Corporate Governance, (1992). **The Financial Aspects of Corporate Governance**, London, Gee (Cadbury Report).

Committee on Corporate Governance, (1998). **Committee on Corporate Governance: Final Report**, London, Gee (Hampel Report)

Cousins, J., Mitchell, A., Sikka, P., and Willmott, H., (1998). **Auditors: Holding the Public to Ransom**, Basildon, Association for Accountancy & Business Affairs.

Cousins, J., Mitchell, A., Sikka, P., Cooper, C., and Arnold, P., (2000). **Insolvent Abuse: Regulating the Insolvency Industry**, Basildon, Association for Accountancy & Business Affairs

Department of Trade and Industry, (1971a). **International Learning Systems Corporation Limited; Pergamon Press Limited (interim report)**, London, HMSO.

Department of Trade, (1971b). **Pinnock Finance Company (Great Britain) Limited**, London, HMSO.

Department of Trade and Industry, (1972). **Pergamon Press Limited (a further interim report)**, London, HMSO.

Department of Trade and Industry, (1973). **Maxwell Scientific International, Robert Maxwell & Co Ltd; Pergamon Press Limited**, London, HMSO.

Department of Trade and Industry, (1976a). **Vehicle and General Insurance Company Limited**, London, HMSO.

Department of Trade and Industry, (1976b). **London and Counties Securities Group**, London, HMSO.

Department of Trade and Industry, (1976c). **Roadships Limited**, London, HMSO.

Department of Trade, (1976d). **Hartley Baird Limited**, HMSO: London

Department of Trade and Industry, (1979). **Burnholme & Forder Limited**, London, HMSO.

Department of Trade and Industry, (1981a). **Kina Holdings**, HMSO, London.

Department of Trade and Industry, (1981b). **Aveley Laboratories Limited**, HMSO, London.

Department of Trade and Industry, (1981c). **Scotia Investments Limited**, HMSO, London.

Department of Trade and Industry, (1983). **Ramor Investments Limited; Derriton Limited**, London, HMSO.

Department of Trade and Industry, (1986). **Regulation of Auditors: Implementation of the EC Eighth Company Law Directive**, London, DTI.

Department of Trade and Industry, (1991a). **Sound Diffusion plc**, London, HMSO.

Department of Trade and Industry, (1991b). **Rotaprint plc**, London, HMSO.

Department of Trade and Industry, (1993a). **London United Investment plc**, London, HMSO.

Department of Trade and Industry, (1993a). **Edencorp Leisure plc**, London, HMSO.

Department of Trade and Industry, (1995). **James Ferguson Holdings plc; Barlow Clowes Gilt Managers Limited (3 Volumes)** London, HMSO.

Department of Trade and Industry, (2001). **Mirror Group Newspapers plc** (two volumes), London: The Stationery Office.

Douglas, M., (1982). **Risk and Blame: Essays in Cultural Theory**, London, Routledge.

Douglas, M., (1986). **Risk acceptability according to the social sciences**, London, Routledge.

Douglas, M., and Wildavsky, (1983). **Risk and Culture**, Berkley, University of California Press.

Dunn, J., and Sikka, P., (1998). The Emergence of UK Auditor Resignation Legislation, **Accounting History**, Vol. 3, No.1, pp. 95-113.

Dunn, J., and Sikka, P., (1999). **Auditors: Keeping the Public in the Dark**, Basildon, Association for Accountancy & Business Affairs.

Giddens, A., (1991). **Modernity and Self-Identity**, Cambridge, Polity Press.

Hall, S., (1997). **Representations: Cultural Representations and Signifying Practices**, Milton Keynes, Open University.

Hanlon, G., (1994). **The Commercialisation of Accountancy: Flexible Accumulation and the Transformation of the Service Class**, London, Macmillan.

House of Commons Social Security Committee, (1992). **The Operation of Pension Funds, Second Report**, London, HMSO.

House of Commons, (2000). **The BSE Inquiry (12 Volumes)**, London, The Stationery Office.

House of Commons Treasury Committee, (1998). **The Mis-Selling Of Personal Pensions**, London, The Stationery Office.

Institute of Chartered Accountants in England and Wales (1986). **A Report of the Working Party on the Future of Audit**, London, ICAEW.

Jenkins, S., (1999). Married to the mob, **The Times**, 3 February 1999, p. 16.

Joint Disciplinary Scheme, (1996). **The investigation of the audits of The International Signal and Control Group PLC**, London, Joint Disciplinary

Scheme.

Joint Disciplinary Scheme, (1999). **Maxwell Investigation – Agreed Statement of Facts, Part 1 and 11** (two floppy disks), London, JDS.

Killick, M., (1998). **Fraudbusters: The Inside Story of the Serious Fraud Office**, London, Indigo.

Lupton, D., (1999). **Risk**, London, Routledge.

Mitchell, A., Puxty, T., Sikka, P and Willmott, H., (1991). ‘**Discussion Paper No. 7, Accounting for Change: Proposals for Reform of Audit and Accounting**’, London, Fabian Society.

Mitchell, A., Puxty, T., Sikka, P., and Willmott, H., (1994). Ethical Statements as Smokescreens for Sectional Interests: The Case of the UK Accountancy Profession, **Journal of Business Ethics**, Vol. 13, No. 1, pp. 39-51.

Mitchell, A., and Sikka, P., (1993). Accounting for Change: The Institutions of Accountancy", **Critical Perspectives on Accounting**, Vol. 4, No. 1, pp. 29-52.

Mitchell, A., Sikka, P., and Willmott, H., (1998). **The Accountants Laundromat**, Basildon, Association for Accountancy & Business Affairs, 1998.

Mitchell, A., Sikka, P., Cooper, C., Willmott, H., and Arnold, P., (2001). **The BCCI Cover-Up**, Basildon, Association for Accountancy & Business Affairs.

Mitchell, A., Sikka, P., Christensen, J., Morris, P., and Filling, S., (2002). **No Accounting for Tax Havens**, Basildon, Association for Accountancy & Business Affairs.

Monbiot, G., (2000). **Captive State: The Corporate Takeover of Britain**, London, Macmillan.

Otley, D.T. and Pierce, B.J., (1996). ‘Auditor Time Budget Pressure: Consequences and Antecedents’, **Accounting, Auditing & Accountability Journal**, pp. 31-38.

Parliamentary Commissioner for Administration, (1989). **The Barlow Clowes Affair**, London, HMSO.

Partnoy, F., (1997). **F.I.A.S.C.O: Blood in the Water on Wall Street**, London, Profile Books.

Pizzo, S., Fricker, M. and Muolo, P. (1990). **Inside Job: The Looting of America's Savings and Loans**, New York: McGraw-Hill.

Power, M.K., (1997). **The Audit Society**, Oxford, Oxford University Press.

Puxty, T., Sikka, P., and Willmott, H., (1994). (Re)Forming the Circle: Education, Ethics and Accountancy Practices, **Accounting Education**, Vol. 3, No. 1, pp. 77-92.

Registry of Friendly Societies, (1979). **Grays Building Society** (Cmnd 7557), London: HMSO.

Reid, M., (1982). **The Secondary Banking Crisis 1973-1975: Its causes and courses**, Basingstoke, Macmillan.

Robson, K., (1991). On the Arenas of Accounting change: The Process of Translation, **Accounting, Organizations and Society**, Vol. 16, No. 5/6, pp. 547-570.

Schlosser, E., (2001). **Fast Food Nation**, London, Allen Lane.

Securities and Exchange Commission, (2000). **Report of the Internal Investigation of Independence Issues at PricewaterhouseCoopers LLP**, Washington DC, SEC.

Sikka, P., (1987). Professional Education and Auditing Books: A Review Article, **British Accounting Review**, pages 291-304.

Sikka, P., (1992). Audit Policy-making in the UK: The Case of "The auditor's considerations in respect of going concern", **European Accounting Review**, Vol. 1, No. 2, pp. 349-392.

Sikka, P., (2001). Regulation of Accountancy and the Power of Capital: Some Observations, **Critical Perspectives on Accounting**, Vol. 12, No. 2, pp.: 199-211.

Sikka, P., Puxty, T., Willmott, H., and Cooper, C., (1998). The Impossibility of

Eliminating the Expectations Gap: Some Theory and Evidence, **Critical Perspectives on Accounting**, Vol. 9, No. 3, pp. 299-330.

Sikka, P., and Willmott, H., (1995a). The Power of 'Independence': Defending and Extending the Jurisdiction of Accounting in the UK, **Accounting, Organizations and Society**, Vol. 20, No. 6, pages 547-581.

Sikka, P. and Willmott, H., (1995b). Illuminating the State-Profession Relationship: Accountants Acting as Department of Trade and Industry Investigators, **Critical Perspectives on Accounting**, Vol. 6, No. 4, pp. 341-369.

Sikka, P., Willmott, H., and Lowe, T., (1989). Guardians of Knowledge and Public Interest: Evidence and Issues of Accountability in the UK Accountancy Profession; **Accounting, Auditing & Accountability**, Vol. 2, No. 2, pp. 47-71.

Simunic, D., (1980). The Pricing of Audit Services: Theory and Evidence, **Journal of Accounting Research**, Spring, pp. 161-190.

Simunic, D., (1984). Auditing, consulting and Auditor Independence, **Journal of Accounting Research**, Autumn, pp. 679-702.

United States, Department of Labor, (1997). **Assessment of the Quality of Employee Benefit Plan Audits**, Washington DC, Department of Labor.

United States, Senate Committee on Foreign Relations (1992). **The BCCI Affair: A Report to the Committee on Foreign Relations by Senator John Kerry and Senator Hank Brown**, Washington DC, USGPO.

Willett, C. and Page, M., (1996). A Survey of Time Budget Pressure and Irregular Auditing Practices amongst Newly Qualified UK Chartered Accountants, **British Accounting Review**, Vol. 28, No. 2, pp. 101-120.

Woolf, E., (1983). Banks: the substance over the form, **Accountancy**, September, pp. 111-112.

Woolf, E. (1986). **Auditing Today (Third Edition)**, Hemel Hempstead, Prentice-Hall.

**ASSOCIATION FOR ACCOUNTANCY & BUSINESS AFFAIRS
PUBLICATIONS IN PRINT**

Dirty Business: The Unchecked Power of Major Accountancy Firms (ISBN 1-902384-07-5) by Austin Mitchell and Prem Sikka

No Accounting for Tax Havens (ISBN 1-902384-06-7) by Austin Mitchell, Prem Sikka, John Christensen, Philip Morris and Steven Filling.

BCCI Cover-Up (ISBN 1-902384-04-9) by Austin Mitchell, Prem Sikka, Patricia Arnold, Christine Cooper and Hugh Willmott.

Insolvent Abuse: Regulating the Insolvency Industry (ISBN 1-902384-04-0) by Jim Cousins, Austin Mitchell, Prem Sikka, Christine Cooper and Patricia Arnold.

No Accounting for Exploitation (ISBN 1-902384-03-2) by Prem Sikka, Bob Wearing and Ajit Nayak.

Auditors: Keeping the Public in the Dark (ISBN 1-902384-02-4) by John Dunn and Prem Sikka.

AABA monographs are priced at £8.95 each and are available from the **Association for Accountancy & Business Affairs, P.O. Box 5874, Basildon, Essex SS16 5FR, UK.**

UK	£8.95 (post free) each
European Union	£8.95 (add £0.65 to cover postage + packaging)
Rest of the World	£8.95 (add £1.20 to cover postage + packaging)

Subject to a modest licensing fee, educational institutions can secure the right to print unlimited number of copies of all our monographs (including those ‘out-of-print’) for an unlimited period. Please write to AABA for details.

<http://visar.csustan.edu/aaba/aaba.htm>

Dirty Business: The Unchecked Power of Major Accountancy Firms shows that the organisational practices of accountancy firms are geared towards advancing their narrow economic interests, often at the expense of wider social interests. The monograph shows that in pursuit of profits major accountancy firms operate cartels, launder money, devise tax avoidance/evasion, bribe officials and obstruct critical inquiries into their affairs. They have been using external audits as a loss leader to sell other services. The internal organisation of accountancy firms encourages falsification of audit work. The absence of ‘duty of care’ to individual stakeholders affected by audits dilutes the economic incentives to deliver good audits. The longevity of auditor appointments encourages personal relationships with company directors. Frequently, audit staff are auditing their one time senior now enjoying a directorial position in a client company. The state and auditing regulators continue to indulge accountancy firms. The cost of this is borne by ordinary citizens who have lost their savings, investments, pensions and jobs.

Austin Mitchell is Labour MP for Great Grimsby. He is a former Labour spokesperson for Trade and Industry. He has written extensively on corporate governance, tax havens, accountancy and business matters in newspaper, magazines and international scholarly journals.

Prem Sikka is Professor of Accounting at the University of Essex. His research on accountancy, corporate governance, money laundering and insolvency has been published in books, scholarly journals, newspapers and magazines. He has also appeared on a number of radio and television programmes.

Dirty Business: The Unchecked Power of Major Accountancy Firms

ISBN 1-902384-07-5

£8.95