

Article
Navigation



Article navigation
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Auditor Litigation Risk and Corporate Disclosure of Quarterly Review Report

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The U.S. Securities and Exchange Commission (SEC) recently made timely reviews of quarterly financial statements mandatory for all registrants. The objective is to improve corporate quarterly reporting. However, formal review reports are not required to be *included* in 10-Q filings, and may not even be issued by auditors. *A priori*, one would expect these reports to be useful to investors if they imply added auditor diligence or if they contain modifications to the standard report. We find that only 5.7 percent of the companies in our sample attached the auditor's review report in their 10-Q filings. Also the majority of these reports are “clean,” suggesting that clients may not be disclosing the reports when they are modified. After controlling for factors such as auditor type, agency costs, capital market transactions, and company size, we find a significant negative association between auditors' litigation risk and disclosure of the review report. In addition, we find that the disclosure of the review report is associated with auditor type and company size.

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The objective is to improve corporate quarterly reporting. However, formal review reports are not required to be included in 10-Q filings, and may not even be issued by auditors. A priori, one would expect these reports to be useful to investors if they imply added auditor diligence or if they contain modifications to the standard report. We find that only 5.7% of the companies in our sample attached the auditor's review report in their 10-Q filings. Krishnan, Jagan and Zhang, Yinqi, Auditor Litigation Risk and Corporate Disclosure of Quarterly Review Report (March 1, 2005). Auditing: A Journal of Practice & Theory, Vol. 24, Supplement, pp. 115-138, 2005, Available at SSRN: <https://ssrn.com/abstract=735943>. Jagan Krishnan (Contact Author). Download Citation | On Jan 1, 2005, Mary S. Stone published DISCUSSION OF Auditor Litigation Risk and Corporate Disclosure of Quarterly Review Report | Find, read and cite all the research you need on ResearchGate. Our study examines the circumstances of non-GAAP financial reporting by 492 U.S. companies that announced restatements from 1995 to 1999. We analyze the occurrence and resolution of litigation over restatements; and, we explore the role of accounting items in bringing and resolving this litigation. To do so, we focus on the income statement. Audit risk is the risk that where financial statements are materially misstated and auditor expresses an inappropriate audit opinion. The risk of material misstatement contains two components, control risk, and inherent risk. Risk of material misstatement in the financial statements explained. Definition: The susceptibility of an assertion about an account balance disclosure or class of transaction to a mistake that could be material, either individually or when complied with other misstatements, before consideration of any other relating controls. Inherent risk describes something about the nature of a business or its transactions that make it particularly susceptible to material misstatements. – Pending litigation and contingent liabilities. Control Risk. Auditor Independence and Audit Quality: A Literature Review. Nopmanee Tepalagul. 1. Therefore, high litigation risk serves as an incentive for auditors to remain independent despite economic dependency. In an early study, Deis and Giroux (1992) document that quality-control review findings increase with the number of clients. Wright and Wright (1997) find that auditors are more likely to waive audit adjustments for larger clients. examining auditors' reporting decisions and the quality of accruals. However, some studies document that NAS increase the likelihood of regulatory investigation and that publicly disclosing NAS fees reduces NAS purchases.