

## LITIGATION

## “The Big Unknown”

By: Keith Langley



Mark Twain said there are “lies, damned lies, and statistics”. Ernst and Young people allegedly lied about not cheating on an ethics exam. EY just agreed to pay \$100 million to settle an SEC investigation into ethics exam cheating. There was an allegation of cheating and failing to report the misconduct. EY has agreed to hire two separate independent consultants to review the firm's ethics and integrity policies and to investigate whether any EY employees contributed to the firm's failure to correct its misleading submission. EY cheated and paid \$100 million – if they did, which other auditors commit similar infractions of their “watch dog” duties? It can be hard to rely on numbers and a “books are good and accurate” representation (see below) by an accounting firm that cheats on an ethics exam. Does this raise a few eyebrows on relying parties, e.g. sureties, who review and rely upon audits, and do not (and cannot) audit the audit?

The U.S. Supreme Court says the auditor is a “watchdog”:

By certifying the public reports that collectively depict a corporation's financial status, the independent auditor assumes a *public* responsibility transcending any employment relationship with the client. The independent public accountant performing this special function owes ultimate allegiance to the corporation's creditors and stockholders, as well as to investing public. This “public watchdog” function demands that the accountant maintain total independence from the client at all times and requires complete fidelity to the public trust. To insulate from disclosure a certified public accountant's interpretations of the client's financial statements would be to ignore the significance of the accountant's role as a disinterested analyst charged with public obligations. *U.S. v. Arthur Young & Co.*, 465 U.S. 805, 817-18 (1984).



Texas • Florida  
Oklahoma • Arkansas

**Texas (Dallas Area)**

8813 N. Tarrant Parkway  
Suite 224  
North Richland Hills, TX 76182  
(214) 722-7160

**Florida (Miami Area)**

P.O. Box 654303  
Miami, Florida 33265

info@l-llp.com

www.langley.law

To "Go Green", our firm uses recyclable paper or ceramic cups and no longer uses Styrofoam cups. In addition, we have adopted a less-paper office environment.

We hope that these changes make big differences in the future.

*Well done is better than well said.*

- Benjamin Franklin



The Restatement of Torts is used by most courts to determine auditor liability, and the 3<sup>rd</sup> edition was recently published, which clarifies a lot of issues. <https://www.ali.org/news/articles/restatement-law-third-torts-liability-economic-harm-published/>. We believe this makes it more difficult for auditors to successfully assert technical defenses to a surety's reliance on the audit.

"Books and Records are Good" – Representation (AICPA / GAAS) language:

We have audited the accompanying balance sheets of X Company (the "Company") as of December 31, 20X2 and 20X1, the related statements of *[titles of the financial statements, e.g., income, comprehensive income, stockholders' equity, and cash flows]*, for each of the three years in the period ended December 31, 20X2, and the related notes *[and schedules]* (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company *as of [date]*

There are three levels of assurance from auditors: audit (highest level of assurance), review (medium level of assurance), and compilation (lowest level of assurance).

A Brief Primer on Suing Auditors by Langley LLP: <https://l-llp.com/uploads/file/A%20Brief%20Primer%20on%20Suing%20Auditors%20by%20Langley%20LLP.pdf>

Keith Langley is a Partner at Langley LLP and may be contacted at [klangley@l-llp.com](mailto:klangley@l-llp.com) or mobile (214) 207-5324.

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