Experiences of auditors and tax advisors with accounting errors: Empirical evidence from the Czech Republic

Experiences of Auditors and Tax Advisors with Accounting Errors: Empirical Evidence from the Czech Republic

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The primary function of financial reports is to represent economic phenomena. A faithful representation of these phenomena is one of the fundamental requirements for financial reporting. Information is expected to be complete, neutral and error free. However, unintentional errors occur occasionally, be it due to incorrect calculations, omissions or due to lack of knowledge of accountants. Auditors and tax advisors are usually the first ones to come in contact with financial reports. They are also usually the first to identify accounting errors. However, neither auditors nor tax advisors are able to identify all errors. Some errors remain in accounting and transitively in the financial statements. This paper focuses on the experiences of auditors and tax advisors from the Czech Republic (CR) with such errors. The paper investigates whether such errors occur, how often they occur, how large they are and how management responds to error detection. The study findings indicate that over 12% of respondents subsequently identify errors in financial statements. Being an auditor or tax advisor does not influence this fact. These errors are generally trivial and appear most commonly among expenses. However, management is not always willing to correct them.

The research objective of this paper is to analyse and evaluate the occurrence of financial statement errors from the perspective of auditors and tax advisors. The research was performed utilising online questionnaires. The questionnaire was prepared in line with the results of previous research (e.g. Adali and Kizil, Emerging Markets Journal, 2017) and pre-tested on a sample of 15 respondents. The final 28-item online questionnaire was fielded in 2019 and took approximately 10 minutes to complete. Respondents were selected using random sampling from the list of CR tax advisors and the CR register of auditors. One hundred fifty-seven tax advisors and 148 auditors were contacted, but responses were received only from only 45 auditors and 57 tax advisors. Only completed questionnaires were retained. The final response rate was 33.4%. Descriptive and mathematical statistics were used to evaluate the data. The chi-square test of independence at a 0.05 significance level and Cramer's V were used to identify the strength of dependence. Size of the errors was classified from insignificant to significant in relation to the total assets of the company. Using this categorization, errors over 1% of assets of the company were considered significant.

Results indicate that 12.7% of respondents encountered a situation where an error was not detected until it appeared in the final financial statements. There was no dependency (p value = 0.2994, Cramer's V = 0.1027) between who identified the error (auditor or tax advisor) and the occurrence of such errors. This result is in line with the findings of Akpanuko and Umoren (Journal of Financial

Reporting and Accounting, 2018). Similar to the results of Turkmen (Procedia Economics and Finance, 2016), such identified errors were generally among expenses (noted by 66.7% of respondents) and assets (37.3% of respondents). This may be because expenses include the most typical accounting errors (e.g. incorrect depreciation, charges or treatment of accruals). Concerning the relative size of the error. Weak statistical dependency (Cramer's V = 0.223) between the frequency of errors and the relative size of such errors was identified (p value = 0.0243). Surprisingly, tax advisors more frequently (p value < 0.0001) than auditors encounter situations where management declines to correct identified errors (Cramer's V = 0.3927). This finding contradicts these of Adali and Kizil (Emerging Markets Journal, 2017), who expected similar rates for both groups. Also, Cramer's V (0.2920) indicated a weak dependency between the average size of errors and management's willingness to correct them (p value = 0.0032). There was no statistically significant difference between auditors and tax advisors in willingness to cover up management's decision to not correct errors (p value = 0.3628).

This paper provides an excursion into the world of auditors and tax advisors and broadens the literature on error occurrence in financial statements. The results show the persistence of errors in financial statements. Several findings were in line with previous research. Interestingly, tax advisors in our sample more frequently encountered situations where management refused to correct errors, which contradicts existing research. We were delighted that most respondents refused to cover up manager's decision to ignore errors in their financial statements as this promotes trust in these professions. The conclusions of this research could be used as motivation for further research on the impact of auditors and tax advisors on the quality of financial reporting.