

Assessing Management Fraud Risk – Are We Skeptical Enough?

Hayes, Thomas, PhD, CPA

University of Arkansas – Fort Smith

tom.hayes@uafs.edu

Abstract

Arguably, one of the most important concepts accounting students learn in their auditing class is professional skepticism. Professional skepticism, which is essentially the auditor's tendency to not accept management assertions without corroborating evidence, is at the heart and soul of every audit engagement. It is a difficult concept to define and measure, yet both researchers and regulators, including the PCAOB, continue to stress the importance of professional skepticism. In our current environment, where the profession continually deals with management fraud concerns, it becomes increasingly important that auditors exercise an appropriate level of skepticism, especially in the planning stages of the audit where fraud risk is initially assessed.

Seventy-two auditing students participated in an experiment where they assessed management fraud risk for a hypothetical company. Participants were first asked to complete a survey that assessed their level of skepticism. Next, they completed the experimental task where they assessed management fraud risk for a company. Results suggest a strong positive correlation between the level of skepticism and the assessed level of management fraud risk. Namely, those participants with a high level of skepticism offered the most conservative assessments of management fraud risk. Implications for practice and future research are discussed in the paper.