Auditing wasn't all Deloitte LLP did for Autonomy Corp., the software firm recently accused of accounting improprieties by its parent company. To many observers, that sort of multitasking is potentially an industry problem.

As auditor, the U.K. unit of Deloitte Touche Tohmatsu was in charge of signing off on Autonomy's financial statements before Hewlett-Packard Co. HPQ -0.95% bought the company in 2011. But Deloitte also was paid significant fees for other work it did for Autonomy, like due-diligence work on a potential acquisition. In 2010, Deloitte received $1.2 million from Autonomy for nonaudit work, close to the $1.5 million the firm was paid for the audit itself.
Non-audit businesses form a steadily increasing portion of Deloitte's business, with 39.6% of revenue now coming from...
consulting or financial advisory, up nearly a third since 2006.

The rise in Deloitte's nonaudit revenue spotlights a recent resurgence in consulting and other nonaudit work by the Big Four accounting firms, a decade after conflict-of-interest concerns and corporate scandal sharply limited such work.

The firms—Deloitte, Ernst & Young, KPMG and PricewaterhouseCoopers—say that their nonaudit businesses operate within legal boundaries, and that their growth isn't cause for concern. They focus their nonaudit work on U.S. companies they don't audit, and on foreign companies that aren't U.S.-listed and thus aren't subject to the U.S. restrictions on nonaudit work.

Even so, the move has revived fears that an increased focus on nonaudit work compromises companies' capacity to sniff out fraud.

"If firms become too preoccupied with consulting, I think it hurts the authenticity of the audit," said former Federal Reserve Chairman Paul Volcker in an interview. Mr. Volcker spoke last week at a New York University roundtable on the comeback of consulting by accounting firms.

Plunging too far into nonaudit services can "distract" firms' attention from auditing and "weakens the public trust" in audits, Paul Beswick, the Securities and Exchange Commission's acting chief accountant, said at an accounting conference Monday. Even if it's only a matter of perception, "negative perceptions can undermine confidence in audits," he said.

The growing focus on consulting and other nonaudit services "threatens to weaken the strength of the audit practice in the firm overall," James Doty, chairman of the Public Company Accounting Oversight Board, the U.S. government's auditing regulator, said at the conference.
H-P alleged last week that Autonomy is riddled with accounting improprieties, though it hasn't alleged any wrongdoing by Deloitte and hasn't cited the firm's dual role as a problem.

Deloitte said much of its nonaudit fees for Autonomy were for "audit-related services" typically carried out by the auditor and actually classified by Deloitte as audit revenues. The firm says it didn't do any consulting work for Autonomy, and that Autonomy had procedures to ensure that any nonaudit services provided by Deloitte didn't compromise its independence.

A decade ago, there was widespread concern that the Big Four would get too cozy with their audit clients because the same companies also were paying them lucrative consulting fees. Those fears peaked when Arthur Andersen imploded after shredding company documents related to Enron Corp.; the auditor made more consulting for Enron than it did for auditing.

The Sarbanes-Oxley Act subsequently barred most consulting for audit clients, and all of the Big Four except Deloitte divested themselves of their consulting businesses.

The firms have since rebuilt those businesses by providing nonaudit services to other companies, within the new prescribed limits. Demand for Sarbanes-Oxley compliance, forensic investigations and merger-and-acquisition work have helped the growth in nonaudit services.

Consulting and other nonaudit lines of business are growing at rates far outpacing auditing. At PwC, for instance, advisory revenue rose 16.9% in fiscal 2012, versus 3.4% for auditing.

"The auditing market is pretty much saturated," said Martin G.H. Wu, an associate professor of accounting at the University of Illinois at Urbana-Champaign. "Consulting, on the
other hand, is pretty unlimited."

If consulting growth continues to boom, the Big Four effectively could become consulting firms that "dabble" in auditing, said Joseph Carcello, a University of Tennessee accounting professor. "I think if we get to that point, we'd have a major, major problem."

The firms disagree. "We wouldn't jeopardize audit quality for anything," said Greg Garrison, clients and markets leader at PwC. "I don't think there's any chance we'd take our eye off the ball, and I don't think our competition would either."

At PwC, 90% of advisory work is for nonaudit clients, said Dana McIlwain, PwC's U.S. advisory leader. The Big Four also argue that consulting provides synergies even if they don't consult for and audit the same companies. Offering consulting gives them expertise they can draw upon when related issues arise at their audit clients, they say.

"We believe the services we're in actually help us on the front of audit quality," said John Ferraro, Ernst & Young's global chief operating officer.

Deloitte could both audit and consult with Autonomy, because it was a U.K. company that didn't trade in the U.S. and thus wasn't subject to Sarbanes-Oxley restrictions. Autonomy paid its auditors about $3.2 million in nonaudit fees over its last three years as an independent company, compared with about $4.5 million in audit fees, according to company filings.

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**QUESTIONS:**

1. Besides auditing annual financial statements, what types of services do public accounting firms provide?

2. Who has recently spoken out against auditing firms providing non-audit services?
What are their concerns?

3. What is the impact of Sarbanes-Oxley on these audit firm activities? Why was Deloitte and Touche not subject to limitations of this law with respect to its work on Autonomy? (Note that Autonomy is the firm purchased by H-P for which H-P recently has taken significant write-downs.)

4. How do you think that the non-audit services provided by public accounting firms might help to improve the quality of audit work also provided by the firm?

5. Consider the possibilities of career advancement in a public accounting firm. Do the consulting services provided by these firms seem attractive to you? Explain your answer.