

Accounting News and Trends

IMPROVED METHOD OF JUDGING INTERNAL CONTROL

A very interesting approach to analyzing internal control is set forth by Mr. James G. Carter in his article "The Internal Triangle" (*The Controller* March 1962). The traditional method of evaluation, the internal control questionnaire, has certain shortcomings that make it difficult for the auditor to construct a total picture of his client's operating processes. Mr. Carter proposes a new technique which he calls the "internal control triangle."

The typical control in cost accounting involves a custodian and a recorder. With proper internal control some independent person would check the other two. The internal control triangle, then, is a triangle that has a custodian operation at the left corner, a recorder operation at the right corner, and, at the apex, an operation that compares the results of recording—the charge or discharge of the custodianship with the actual balance of the physical assets on hand. The purpose of visualizing this triangle is to focus attention on people and the tasks they perform, and to prompt the auditor to ask himself questions, the answers to which will determine the degree of test checking or detailed

vouching he will have to do to form an opinion.

The paper flow in a well-organized business is by functions. Accounting control of this paper flow usually recognizes five functions: receiving cash, paying out cash, buying and selling material and the buying of labor services. For each function of the business the auditor should try to determine the existence, in whole or part, of a process triangle.

If there is a triangle for each of these functions, he should then settle in his mind an opinion as to what operations form the key process triangle for each function. Sometimes a function may have more than one key process triangle. In addition, accuracy may have one triangle whereas fraud may have a slightly different triangle. The poorer the system of internal control, the more the auditor is concerned with the fraud triangle. The critical point in the fraud triangle is the accurate performance of the key tasks by the people involved in the three operations. The reliance upon the triangle depends upon the diligence with which the key tasks are performed.

The author gives many specific instances of how to apply this approach. He believes that the soon-acquired ability to sort out and label the key triangles gives "direction, momentum and scientific precision to a professional art. The triangle concept is the key that releases the auditor from the dull bondage of the footing, checking and examining procedures emphasized for years and allows him new intellectual status and mental stimulation in the performance of his important duties."

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Various comments in *The Accountant* (Great Britain) present a summary of the status of University accounting education in the United Kingdom. Since the pattern is modeled after that in many parts of the United States, it may be of interest to consider it.

Toward the end of World War II a committee representing the various accounting associations recommended the setting up of university degrees suitable for future accountants. Such degrees were to have accounting, economics, and law as their main subjects, and were also to include courses in related topics such as government. Twelve universities agreed to set up such degrees, and the scheme was launched soon after the war. Graduates under the scheme, like other graduates, serve "articles" for only three years; unlike other graduates, they are exempt from the professional intermediate examinations, but, of course have to take the final examination.

Recently a special committee reviewed the situation and reached a somewhat tepid verdict: "The only conclusion we can reach is that even after fifteen years there is still not enough evidence to show whether in general the scheme should be encouraged or abandoned or changed or left as it is. We therefore favour leaving it substantially as it is pending still further experience of its value." The reason for this lack of enthusiasm seemed to be in part based on the fact that while those with the special degree did better than those with no degree on the Final Professional Examination, they were somewhat less successful than holders of other degrees. Since the statistics were limited to one year and since only 42 special graduates were involved, the study had obvious

flaws.

The editorial comments pointed out that criticism of the scheme came from two diametrically opposed points of view: some employers complain that the new graduate is initially less useful in the office than the clerk with three years of audit experience; others attack the special degree because it is too practical. This latter group states that students should seek breadth by reading some subject remote from accounting in which they happen to have a special interest. There is at least one more argument for the special degree, according to the editorial writers and it is:

"Accounting—as a profession and an area of knowledge—is surely important enough in its own right to deserve critical study by outside scholars. American experience has shown that such study can, by a feed-back process, contribute to practice—that universities produce new accounting as well as new accountants. It would be strange if Britain, too, did not gain by fostering strong schools of accounting in her universities."

AUDIT SAMPLING IN ACTION

The Federal Government Accountants Association recently issued its Research Bulletin #1 having the above title. It briefly explains certain statistical sampling concepts and includes case studies illustrating techniques with respect to travel expense vouchers, stock inventory records, confirmation of unpaid mortgage balances and other items. This bulletin should have utility in industry audits.

A GUIDE FOR AUDITING AUTOMATIC DATA PROCESSING SYSTEMS

The Air Force's Auditor General recently issued a booklet having the above title. Though prepared for Air Force auditors it undoubtedly will