Journal of Accountancy

Volume 46 | Issue 3 Article 2

9-1928

Accountants' Responsibility for Inventory Verification

C. O. Wellington

Follow this and additional works at: https://egrove.olemiss.edu/jofa

Part of the Accounting Commons

Recommended Citation
Wellington, C. O. (1928) "Accountants' Responsibility for Inventory Verification," *Journal of Accountancy*: Vol. 46 : Iss. 3 , Article 2.
Available at: https://egrove.olemiss.edu/jofa/vol46/iss3/2

This Article is brought to you for free and open access by the Archival Digital Accounting Collection at eGrove. It has been accepted for inclusion in Journal of Accountancy by an authorized editor of eGrove. For more information, please contact egrove@olemiss.edu.

Accountants' Responsibility for Inventory Verification

By C. O. Wellington

Now that the December 31, 1927, statements are well behind us and there is a breathing spell it may be worth while to consider again the responsibility the public accountant should take in verifying and certifying to inventories as part of a balance-sheet. There is a regrettable lack of uniformity among members of the accountancy profession in practice and preaching on this subject. On the one hand we have the belief that "verification of physical inventories is not within the competence of auditors"*; and on the other several statements by well-known accountants that indicate a desire to accept greater responsibilities for inventory verification.

Indeed there is a maze of controversial statements on the subject, owing largely to the fact that both proponents and opponents of inventory verification have talked in generalities, and the exact points of difference have seldom been clearly indicated. So in presenting my own views on the subject, I desire most of all to define the fundamentals so clearly that one can hardly fail to understand the real issues.

RELATIVE IMPORTANCE OF INVENTORY ITEM

At the outset we must recognize that the inventory, in the case of the average manufacturing or trading concern, is an item of major importance. Owing to variations in types of business, different rates of turnover and fluctuations in general business conditions, the exact weight of the inventory item on balance-sheets is variable. An instance comes to mind of a tannery with an inventory of $750,000 out of total assets of $1,000,000. This is an extraordinary example and usually the inventory is of less comparative weight, but in most cases it represents 50 per cent. of the current assets.

Moreover, no other single item in the balance-sheet lends itself more readily to misrepresentation, or is more affected by optimism or an unwillingness to face unpleasant facts—or, when the personal interests of the client are better served, by excessive conservatism. Then, too, no other item is more difficult to verify. The examination of cash, notes receivable and accounts receivable and the veri-

* From an address by George O. May before the Society of Certified Public Accountants of the State of New Jersey, quoted editorially in the April, 1927, issue of The Journal of Accountancy.

fication of notes and accounts payable are simple in comparison with the count and the valuation of raw materials, work in process and finished goods.

ATTITUDE OF BANKERS AND BUSINESS MEN

In view of the intrinsic importance of the inventory item, and the comparative difficulty of obtaining a satisfactory verification, bankers have naturally developed an interest in the relationship of auditors to inventories. Three decades ago banking was more on the basis of personal relationships, and few borrowers were required to submit financial statements. With the growth of business concerns and banks and the development of credit analysis, however, bankers have come to realize the value of certified statements, but at the same time they have looked with an increasingly critical eye upon the treatment of inventories in such statements.

Bankers are concerned with quantitative aspects of an inventory—whether it is excessive, normal or depleted—because of the effects upon cash, turnover, purchasing, etc. Likewise they are interested in qualitative aspects—whether stable, perishable or obsolete—because of the effects upon sales. Before bankers can reach any sound conclusions on either quantitative or qualitative points, however, they need the fundamental assurance of accuracy in count and valuation. Over the last few years there have been many cases of large concerns failing for huge sums, where the inventories as shown by the last public statements were grossly overstated. Is it any wonder that for assurance against such a possibility bankers should look to the auditor, a disinterested professional man who is on the ground? Is it any wonder that they should desire to know exactly what he did to verify the inventory; or, if he did nothing, why he passed over such an important item?

This attitude on the part of bankers is not imaginary. Some time ago Walter H. Sachs said, in terms unmistakable to all who were willing to understand, that in the opinion of bankers auditors ought to assume responsibility for inventory verification. The matter now is even more alive than ever. In obtaining material for this article, I have talked with a number of bank credit men, and I have learned that some, because they know so little and can find out so little about the inventory in the average case, omit it from the current assets and lend on the basis of cash and receivables only. And the recent report of the Robert Morris Associates committee on coöperation with public accountants closes with

these words: "It is our firm conviction that, as time goes on, accountants should be held to a greater rather than a lesser responsibility as concerns this very important item." I believe these expressions of opinion indicate accurately the attitude of the bankers and that public accountants must recognize the situation, whether they like it or not.

Business men, too, although not interested in inventory technicalities to the same extent as bankers, have become educated, through contacts with bankers and through their own observations, to the importance of proper inventory verification (even if they may be reluctant to admit the necessity in their own cases). Looking at the matter from a common-sense point of view, they simply assume that an auditor ought to be able to verify inventories as well as any other balance-sheet item. With the value of auditing services pounded into their heads for years, is it any wonder that they do not recognize in connection with inventory verification any limitation upon the skill and ability of auditors?

Inventory verification, therefore, is not merely an academic issue. The relative importance of the inventory item, and the natural attitude of bankers and business men toward it, raise practical questions which every conscientious auditor has to face, namely:

1. Should the auditor assume responsibility for inventory verification?
2. If so, what procedure should he follow?

OBJECTIONS FREQUENTLY URGED

In reaching a decision on these points, auditors sometimes attach too much importance to objections based on out-of-date facts or illogical generalities. They do not strip away the superficialities and get down to the real issue in its present-day aspects.

It is frequently urged, for instance, that according to British court decisions "it is no part of an auditor's duty to take stock." Auditors' responsibilities are doubtless heavy, and they are naturally disinclined to enlarge their work unnecessarily. On the other hand, the profession has grown away from various restrictions of old British practice; during the last twenty years professional opinion has approved the assumption of responsibilities theretofore deemed utterly unreasonable. Legal decisions obviously lag considerably behind professional developments, and at present there is no reason to restrict an auditor's responsibility except through his own standards. Indeed, the assumption of responsi-

bility by the present-day auditor is limited only by his professional skill.

Another objection—corollary to that above—expresses the old-school idea that the auditor should depend on the honesty of his client for a correct inventory and that if there seems to be any ground for suspicion he should refuse to handle the case. As a sound means of verification, however, reliance upon the client's honesty is no more justifiable in the case of inventory than in the case of cash or accounts receivable. Passive withdrawal from an engagement is a poor substitute for an audit well performed.

It is frequently contended that in very few cases does the auditor have the opportunity to verify quantities and that too often the size of the inventory and the limitations of time and expense imposed by the client prevent a satisfactory verification. Somewhat similar in nature is the argument that the auditor can not serve two masters and that between the banker who desires inventory verification and the client who refuses it the auditor occupies a most unpleasant position. These are arguments of expediency, not touching the fundamental issue. If the auditor ought to assume responsibility for inventory verification, his inability to obtain the proper authority, through timely negotiations, is not a valid argument against trying in general; it is merely a case of failure in particular, excusable or inexcusable according to circumstances.

Again, it is argued that the auditor is not competent to verify an inventory and that there have been few cases of inventory overstatement which would not have been disclosed by an ordinarily efficient audit. These are objections which are untenable because of their very generality. Before one is justified in expressing any conclusion as to the competency of auditors, he should get down to particulars and consider what a really satisfactory inventory verification requires, what is done in the "ordinarily efficient audit," and what more, if anything, would have to be done to permit an assumption of full responsibility.

VARIOUS POSSIBLE RELATIONSHIPS

Let us examine the various relationships that may exist between an auditor and his client with regard to inventories and see what he may do by way of verification in comparison with what he ought to do.

In general, the situation may well be summarized as follows:

Circumstances	Degree of auditor's responsibility	Desirability
1. Inventory determined by client and used without verification.........	None	Minimum
2. Inventory taken and priced by client, but tested (after taking) by auditor	Limited	Medium
3. Inventory taken or supervised by auditor.........................	Full	Maximum

NO VERIFICATION BY AUDITOR

Cases where the auditor uses without any verification the inventory as determined by his client are sometimes the natural result of the special type of work undertaken. In the case of a proposed merger or consolidation, for instance, the major significance attributed to earning power sometimes leads to a mutual acceptance of inventories without any verification by the auditor. That such a practice is dangerous and should not be followed is clearly shown by cases where trouble has developed shortly after the auditors have prepared statements in connection with new financing, and disclosure of a substantial overvaluation of inventories has led to severe criticism of the auditors—whether they were wholly to blame or not. Most cases of absence of verification, however, are the direct result of a refusal of clients to permit such work, regardless of the relative importance of the inventory item.

Where the auditor is not permitted to take any steps to verify the inventory, his only recourse is to qualify his certificate so as to indicate unmistakably that his determination of the true financial condition is limited by acceptance of the inventory as determined by the client. The auditor has a duty to himself to put any reviewer of the balance-sheet definitely on notice as to the incompleteness of his audit procedure. Conversely, the reviewer of the balance-sheet has a right to know this fact.

QUALIFIED CERTIFICATE THE LAST RESORT

Where an inventory verification ought to be made—and such is true in most cases—the use of a qualified certificate should be viewed by the auditor as the last resort in lieu of something better. However extenuating may be the circumstances arising from the client's limitation, and however well fortified from the legal point of view the auditor may be with an inventory certificate signed by the client, the situation can hardly satisfy the conscience of the

progressive auditor or appeal to the common-sense of statement analysts.

The impression upon the general public, too, is detrimental to the best interests of the auditor and his profession. If there is the least intimation that the auditor is looking upon a certificate from the client as anything more than a legal safeguard, the public is prone to jump to the conclusion that the auditor carefully and gladly avoided something about which he knew nothing, and other items on the balance-sheet become tinged with suspicion. Moreover, when newspapers feature frauds discovered in unverified inventories, the public thinks nothing of qualified certificates, but it considers the mere signing of the auditor's name to the statement as discreditable to him and to his profession. Unfair? Yes—but only the more reason why the auditor should deal with unverified inventories only with the greatest reluctance and after exhausting every possible means of converting his client to a better appreciation of the highest professional standards.

INVENTORY TESTS BY AUDITOR

We come now to the second general type of circumstances—where the inventory is counted, priced, extended and footed by the client, but is later subjected to certain tests by the auditor. The exact character of these tests varies with individual auditors and individual cases, but merely as an illustration of the general scope, the following activities may be mentioned:

1. Obtaining copy of completed inventory, and test checking to original count records, however crude, and to perpetual inventory records.
2. Considering ownership of goods:
   - (a) In warehouses
   - (b) At other plants (e.g., dye-houses)
   - (c) On consignment
   - (d) Under pledge as security for loans
3. Checking inventory cut-off:
   - (a) Goods on hand—liability not on books
   - (b) Goods not received—liability on books
   - (c) Goods shipped—not billed
   - (d) Goods not shipped—billed
4. Verifying valuation at cost or market, whichever is lower:
   - (a) Test checking raw-material prices against original and current invoices
   - (b) Test checking costing of work in process and finished goods
   - (c) Examining pricing of depreciated or obsolete stock

5. Test checking extensions and footings.
6. Comparing total inventory with business done, through tests of gross profit, quantities received and delivered, rate of turnover and other similar tests.

No hard and fast rule exists as to the extent of the test checks to be made. The value of the client's internal checks, the extent and the accuracy of the cost system, the availability and the worth of collateral evidence—all have their bearing. In general, however, the theory is that the auditor shall perform sufficiently extensive tests to satisfy himself as to the substantial accuracy of the inventory and that, if more work along any one or more lines is demanded by errors discovered, he shall pursue his verification, after explanation to the client, to the point where further errors will probably be relatively negligible. In other words, the responsibility of the auditor increases rather than diminishes with extra work required by circumstances.

With his tests completed in a manner satisfactory to himself, the auditor is then prepared to assume a responsibility for the inventory limited only by his acceptance of the *quantities* as certified to him by the client.

WEAK POINTS IN ORDINARY PROCEDURE

One practical defect in the application of this theory is that the auditor, unduly conscious of his limited responsibility, allows his tests to deteriorate in quantity and quality. There is too much of a tendency to look upon the work as the job of juniors, and to take the inventory sheets as prepared by the client, give prices of raw materials a few cursory glances, check the mathematics on items which run into money and let it go at that. This results in ignoring small items, which may be greatly overvalued or undervalued; in not giving proper consideration to unsalable stock, and in largely disregarding the pricing of work in process and finished goods. Limited responsibility is too likely to result in slackness.

The primary difficulty with ordinary inventory tests, however, is that the absence of a check on quantities leaves the question of understatement or overstatement wholly undecided. If a client lists 20,000 pounds of linotype metal instead of 2,000, either through accident or design, of what avail is verifying the price at 12 cents and extending the value? Or of what real use is it for the auditor's assistants to correct errors of $2,543.86 in extensions and footings, when the total inventory may be $25,000 over or under, owing to the use of incorrect quantities?

It would be difficult for the officers of a company to organize a conspiracy throughout the plant, so that men could take an inventory incorrectly and alter plant records without detection. It would be easy, however, for the officers in collusion with a few office clerks to mark up inventory quantities so as to perpetrate fraud on a large scale. In the Hamilton Manufacturing Company case, stock in process was carried at $1,207,290, but an actual count later by auditors showed a correct inventory of only $234,542, inventory reports from mills having been raised at the general office. In a recent case an inventory valued at $2,400,000 was overstated $1,100,000, the auditors having merely accepted some neatly typewritten sheets and made some mathematical tests. They did not even reconcile the factory ledger and the general ledger, although these were much out of balance due to irregularities.

But, it is asserted, these are only a few sporadic cases, and only the most dishonest executives would be guilty of such fraud. In the case of smaller companies, where deliberate falsification is more easily effected, frauds are not common, and grantors of credit might well seek protection in a distribution of risks and the law of averages. Sorry, sorry arguments! If inventory frauds are made possible by the absence of verification of quantities by auditors, the important question is not how much the frauds amount to, or how often they occur; not how grantors of credit can spread their losses—but how auditors can prevent such frauds.

It is not wholly satisfactory to depend upon a verification of inventory quantities and price through checking the total inventory value by the gross-profit test. In an enterprise where the gross profit remains fairly constant, this test will suffice to show any abnormal change in the rate due to fluctuations in costs or selling prices or to errors or fraud in stock-taking. In other words, the test merely points out a discrepancy; it does not automatically indicate the precise cause. By making a detailed investigation, varying in complexity with the nature of the business, the auditor may be able to satisfy himself as to the change in gross profit properly attributable to new costs or selling prices, but too often the client presents what it insists is a reasonable explanation, and the auditor does not consider it expedient to carry his investigation further. In cases where there seems to be no cause contributing to a change in gross profit except inventory errors or fraud, the auditor can not well stop at this point. To reduce his general suspicion to facts he must request a new physical inventory under

his supervision, and then work back, by adding quantities sold and deducting quantities purchased, to determine the proper inventory figure at closing.

All in all, ordinary inventory tests produce an indefinite verification unless they are pursued to the point where the auditor supervises a post-closing inventory and works back to the closing figure. In such cases it would have been better for all concerned if the auditor had taken or supervised the closing inventory—easier and more effective for the auditor and less expensive to his client. It is said that the auditor's position should be definite. A most sound premise—but the proper conclusion is definiteness in favor of direct quantity verification, rather than any roundabout procedure or an unquestioning acceptance of quantities from the client.

Bankers and business men in general feel that no matter how well the "ordinary tests" are performed there is a vital weakness in an inventory certification which does not cover quantities, and that the auditor should do everything in his power to measure up to his opportunities by verifying quantities also. Otherwise his certificate is only of medium worth.

INVENTORY TAKEN OR SUPERVISED BY AUDITOR

The third typical situation is where the auditor is directly responsible for actually taking the inventory or intimately supervising it. The occasionally expressed conviction that the auditor is not really competent to carry such work to a successful conclusion is due at least in part to the lack of a clear understanding as to what such work properly means. Substantially it means this:

1. Pre-inventory
   - (a) Arranging with client as to date, and shutdown of operations
   - (b) Determining kind of tags and inventory sheets
   - (c) Having tags properly numbered
   - (d) Issuing instructions for their use and return, used or unused
   - (e) Arranging for listing of tags on inventory sheets, for pricing and for extending
   - (f) Arranging for suitable internal checks
2. Inventory
   - (a) Supervising inventory procedure, to see that it is functioning properly
   - (b) Taking inventory tags after listing, and making test counts

(c) Test checking tags to duplicate set of inventory sheets, to be retained by the auditor
(d) Giving special attention to goods in shipping and receiving rooms
(e) Inspecting inventory groups for unsalable stock

3. Post-inventory
   (a) Comparing client's official inventory sheets with auditor's duplicate set to check additions, eliminations or alterations of quantities
   (b) Continuing with the test checks previously outlined for the ordinary audit

From the foregoing outline it will be apparent that the auditor, in assuming full responsibility for inventory verification, departs from what has been called "ordinary" audit procedure only in that he participates directly in pre-inventory work and in the counting on the inventory date. Now why is he not competent to do this?

NOT COMPETENT TO ARRANGE PROCEDURE!

Whether or not the auditor needs to organize the entire procedure for inventory-taking depends, of course, on what the client already has available. Perhaps the auditor will find it necessary only to make certain improvements in practices formerly used by the client. But whether the pre-inventory work requires a complete system installation or merely the perfection of previous methods, the auditor ought to be competent to do the job.

Admittedly auditors vary in their abilities to devise new or improved accounting methods. In other words, some are better qualified than others by training and experience to deal successfully with problems of constructive accounting, as contrasted with analytical accounting. Whatever may be the gradations of skill required to handle various aspects of constructive accounting, however, it can not be believed that any really qualified practitioners are incapable of making original installations of sound methods for inventory taking, or recommending necessary improvements in methods formerly used by the client.

NOT COMPETENT TO COUNT!

And why should not the auditor be able to count inventory items? One might dismiss the question simply with the observation that the auditor who is unable to identify articles by the descriptions on the inventory tags, as a preliminary move to making himself reasonably certain about the quantities on hand, is equally unable to be positive that the articles are properly

priced. The wording of invoices or trade-paper reports, and changes in goods during processing are all likely to involve variations in descriptive terms, and it is no more difficult for the auditor to know what he is counting than it is to know what he is pricing. Denial of the ability to count, therefore, is a denial of the ability to price—that so very important phase of "ordinary" inventory verification.

Nevertheless, accepting the statement that the auditor is not competent to count as a logical objection, let us translate it into what is really meant—namely, that the auditor, in counting, may be confronted with annoying difficulties. Barrels of oil may be full—of water; boxes of books may be full—of waste paper and waste type-metal. Grain, pig-iron, sand, coal, logs are not easy to measure or count, and what endless days would be required to determine the quantities of seeds in the case of a flower and vegetable seed dealer, or the number of minute screws and other parts in a watch factory! All true, but inconclusive.

In the first place, no banker or any one else expects the auditor in most cases to compute the quantity of every item of inventory. Under extraordinary conditions he and his assistants may be called upon to take the entire inventory, without any help from the client's organization, but as a rule his verification of quantities consists of making an adequate number of tests to satisfy himself as to the substantial accuracy of the client's counting. It is no more necessary for the auditor to count every item than it is for him to check every footing and posting in the books of account. The complete verification of every transaction is not the goal of even a detailed audit, for the modern rule clearly prescribes only reasonable checks, sufficiently extensive in view of conditions disclosed to warrant faith in the general accuracy of the records. So, in the case of inventories, an exact count of a reasonable number and variety of items, coupled with a general inspection of the others, is all that is needed to satisfy the auditor in assuming responsibility for quantities.

In the second place, in making his tests the auditor will naturally resort to all the protective, time-saving and labor-saving practices that are characteristic of professional skill. Test openings of barrels and boxes, and test drilling in raw-material piles, made by the client's employees under the auditor's supervision; applications of formulas for transforming cubical contents into weights; counting the number of items in a standard space—such

means are simply the expression of the auditor's expected ability. Certainly the auditor would never count every sheet in a pile of 25,000 flat-sheets of a book in process, when he could count one layer, or a basic quantity of say 500 sheets, and obtain a very close approximation of the total by inspection. Thus the work of the auditor in verifying quantities consists partly in actually counting, but, to a more important extent, in formulating and applying various standards of judgment to minimize the work without detracting from the reasonable effectiveness of the check.

It should be remembered that records of the client may not be without value in verifying the inventory quantities. For example, wool, cotton, hides, etc., are commonly handled by rigid lot records, and it would be inexcusable for any auditor not to utilize these to supplement his counts in verifying what is on hand. Likewise, where the client uses continuous inventory records, tied in with cost and production records, the relationship of the quantities on these records to the test counts of the auditor ought to be an important factor in the determination of his final opinion as to the substantial accuracy of the physical inventory as a whole.

Truly the auditor ought to be able to go beyond the limits of "ordinary" procedure, and not only formulate proper arrangements for taking the inventory, but also make a satisfactory verification of the quantities. He can then give an unqualified certificate, which is of maximum worth.

QUESTION OF UNSALABLE STOCK

One further point regarding competency, however, remains to be discussed. The "ordinarily efficient audit," as commonly outlined, provides for a check against the excessive valuation of stock which is not readily salable because of depreciation or obsolescence; yet inability to perform such work satisfactorily is often advanced as an argument against assuming full responsibility for inventory verification. As stated before, many "ordinary" audits are defective in their consideration of unsalable stock, without any corresponding qualification of the auditors' certificates, and one is hardly justified in upholding the "ordinary" audit as a completely satisfactory model and at the same time raising a defect therein as an argument against assuming full responsibility.

As a matter of fact, although an auditor may encounter difficulties in judging unsalable stock at his first audit, they are not

insuperable, and they become less with repetitions of the work. Does it require any unusual perspicacity on the part of the auditor to decide that goods are not worth their cost in cases such as these:

1. When a publishing house prints 50,000 copies of some sensational war memoirs, and sells 20,000 copies within two months and practically none in the next six?
2. When a worsted-goods mill has hundreds of pounds of fancy yarns, and has almost entirely turned from making mixed goods to plain goods?
3. When a corset manufacturer has a stock of "steel-cages" mixed in with the elastic "wrap-arounds" now in vogue?
4. When a radio manufacturer still has some multiple-control, transformer amplified sets alongside his new single-dial, impedance-coupled models?

It is not to be supposed that the auditor will have as intensive a knowledge of sales conditions as the sales manager of his client; but from his general business knowledge, from his acquaintanceship with his client's operations, market and turnover, and from information derivable from inactive stock accounts and low rates of turnover, he ought to be able to reach definite conclusions as to what goods need low valuations because of unsalability. In special cases, in order to determine the relative probability of the usual profitable conversion and sale, the auditor can age the inventory by classifying current and old materials, and also ascertaining what old materials are being requisitioned for current orders.

WHEN CLIENT DENIES ERROR

It is frequently contended that when the auditor does assume full responsibility for the inventory, he may come into conflict with his client because the latter refuses to recognize a material error in valuation, especially in connection with unsalable stock. It is to be feared that such a question is too often decided upon the basis of expediency; but in theory there is no reason why the auditor should not insist upon using a valuation satisfactory to himself, setting up an inventory reserve in his report if necessary.

Exactly the same situation may arise in the course of an "ordinary" audit. Suppose the client insists on a reserve for bad debts which is grossly inadequate in the opinion of the auditor. Would the auditor be justified in using the client's valuation without comment, or even in qualifying his certificate to cover an

acceptance of accounts receivable as valued by the client? Where the auditor is reasonably positive that inflated values are used, it is his duty to show what in his opinion are the correct values. If expediency results in compromise, his professional standard has been lowered; his obligation has remained unchanged.

COST NOT UNREASONABLE

It may be useful to throw the light of experience upon the contention that the assumption of full responsibility for inventory verification would mean greatly increased fees to clients, out of all proportion to the benefits to be derived. It is often argued that between an enormously costly "complete" audit, unnecessary in most cases, and a cheap superficial audit, wasteful and dangerous, there is a golden mean where an audit wholly justifies its cost. But does it follow, as inevitably as night follows day, that inventory verification is automatically excluded from this golden mean?

There certainly are degrees beyond which the auditor can not reasonably ask his client to spend money, and no sane auditor extends the scope of his audit procedure unduly. No sound reason exists, however, why the auditor should not urge his client to spend money on the matters that really count. An enormous amount of time is devoted by auditors to what Kipling calls "footing and carrying one," when what is really wanted is a reliable answer to the question: what are the values there? Auditing practice as a whole spends too much time on checking postings and running down 23-cent errors in bank balances, while considering that an inventory within 15 per cent. or 20 per cent. is close enough. The vital point, therefore, is not how much inventory verification would increase the cost of audits, but how auditors are going to meet fully the responsibility of so organizing and conducting their work as to make it count for the most to their clients.

As to the intimation that only benefits of slight if any value result to the client from inventory verification, the answer is self-evident: if verification confers no benefits in the case of an item which usually represents 50 per cent. of the current assets and has involved the grossest frauds and the worst displays of unfounded optimism, then are any worthwhile benefits to be derived from verification of other items? Then what price auditing?

The fact is that the auditor can make inventory verification an integral part of his programme without undue cost to the client. We know from experience that we can assume full responsibility for from 30 per cent. to 50 per cent. of the audit fee—the exact amount in any case depending, as it should, upon the relative importance of the inventory among the items to be verified. Fees certainly do not have to be "multiplied," as some accountants have claimed would be the case.

Upon this basis we have emphasized to clients the importance of our assuming full responsibility for inventory verification, and we have met with a gratifying response. Some clients, it is true, look with a cold eye upon the proposition, but what professional man has not encountered individuals who are slow to become educated to the value of professional services? If the refusal of a client to buy a particular form of service were to constitute a sound criterion for judging that service to be generally excessive in cost and useless in results, it would be thumbs-down for every professional activity on earth. The clients who do buy the service and continue to buy it are the real test.

GROWING WILLINGNESS TO TAKE RESPONSIBILITY

A few decades ago auditors were told emphatically not to touch inventories, but a feeling has developed that this constitutes a lax point in auditing practice. I believe that were a thorough canvass to be made among auditors of high standing in the profession, a surprisingly large number would be in favor of exercising full responsibility for inventory verification—not merely accepting it, but demanding it. They are not insurers, but they do feel competent to express reliable opinions.

It is much to be suspected that bankers who wish auditors to verify inventories do not always direct their emphasis at the right parties. In other words, it is barely possible that a banker may feel constrained to bow to the dictates of expediency in dealing with a certain borrower, and then be inclined to blame the auditor if the latter is unable to sell the idea of inventory verification. This much certainly is true—that any banker who seriously wants an inventory verification, and will strongly support the idea, can find more than one auditor who is qualified by training and experience to perform this work satisfactorily and, far from shirking the task, will welcome it.