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CERTIFIED PUBLIC ACCOUNTANTS

BULLETIN

EXECUTIVE OFFICES
30 BROAD STREET, NEW YORK

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Vol. IX

NEW YORK, OCTOBER, 1926

No. 10

Annual Meeting

AMID the din of pneumatic hammers and other apparatus being used in the construction of two nearby skyscrapers, the 1926 annual meeting of members and managers of the firm was held at the executive offices on September 16, 17, and 18. Despite this extraneous noise, it was agreed unanimously that the meeting was one of the most enjoyable and successful in our history.

All of the firm members, now numbering twenty-eight, were present. Mr. Kracke, who was unable to attend last year's meeting because of the pressure of engagements at the Berlin office, deferred his pending return to Germany in order to be present at this year's meeting.

All of the thirty-two American practice offices were represented except Birmingham. Mr. Hammond found it impossible to leave that office because of an important engagement to which he was giving attention. Of the four foreign offices, London and Paris were not represented. Mr. Kracke represented the Berlin office, and Mr. B. A. Padon the Shanghai office. Mr. Padon, who has been associated with our practice in China since 1919, is making, with his family, his first visit to this country in three years. He will return to Shanghai after a vacation here, to resume the management of our office there.

The program inaugurated successfully last year was used again this year with equally good results. The first day, Thursday, was given over to informal gathering and individual conferences and discussions. A buffet luncheon was served at noon in the library. In the afternoon a conference of partners was held in Mr. Ludlam's office. In the evening there were a number of private dinners, followed by a theater party, the attraction being "The Great Temptations."

On Friday the golf tournament—which has come to be an annual classic—was held at the Garden City Country Club. After a day of severe competition, Mr. Jumonville emerged victorious with a low net score of 72, thereby retaining the crown which he won last year. With a card of 83, Mr. Lawrence acquired the laurels for low gross, which Mr. Morris won two years ago and defended successfully last year. Mr. Kracke was awarded the consolation prize. We shall not mention the score.

A dinner and dance, attended by the partners and managers and their wives, followed the golf tournament. It was unanimously conceded to be the most pleasant social event in the history of our annual meetings.

Saturday, the third day of the meeting, was devoted to more serious matters. A

professional conference and business session, at which Mr. Ludlam presided, was held in the library in the morning and again in the afternoon. Various discussions were had, of technical questions and of matters relating to practice office management, general administration, and relations with clients.

The important question of service classification and its application to reports occupied most attention, the entire morning session being given over to a discussion of matters pertinent thereto. Mr. Wildman presented a digest and summary of the replies to the questionnaire sent out recently by the executive offices in order to ascertain the experience of the practice offices in the application of the service classification promulgated last winter.

The results of the questionnaire indicated that all persons in the organization agreed that the service classification had been of great assistance in helping them to think more clearly concerning the character, scope, limitations, etc., of the various types of engagements which the firm is called upon to perform. There was unanimous agreement also that the service classification had helped, in taking engagements, to arrive at a better understanding with clients as to our service.

The principal difficulties encountered in connection with the service classification concerned the first four service classes, namely, general audits, balance sheet audits, cash audits, and general examinations. It is believed that the difficulties will be largely overcome by more lucid and ample description of the services comprehended under these heads, particularly 1, 2, and 4. Mr. Wildman announced the proposed revision of the text applicable to the first four service classes as follows:

1. *General Audits.*

A general audit comprehends verification of the assets, liabilities, capital, and surplus as of a given date, and of the

cash receipts and disbursements, income, expense, and miscellaneous profits and losses for a period ended on that date, together with the preparation of an audit report, with or without a certificate.

This type of service contemplates that the accountant, in addition to verifying balances at a given date, shall satisfy himself reasonably as to the transactions resulting in such balances and as to the accuracy of the records.

2. *Balance Sheet Audits.*

A balance sheet audit comprehends verification as of a given date of the assets, liabilities, capital, and surplus, including as an incident thereto, such examination of the operations as may be necessary to give credence to the stated financial condition, and the preparation of a report containing a balance sheet which may or may not be certified. If a statement of income and profit and loss is included in the report, it should be qualified as having been prepared from the books without verification.

This type of service, while contemplating certain examination of the records with a view to substantiating the assets as represented and affording reasonable assurance that there are no liabilities (actual or contingent) other than those admitted, does not comprehend systematic verification of transactions, such as is required in a general audit, and therefore may not be relied upon to disclose any understatement of assets which may have been concealed in the operating accounts.

Restriction in the verification of one or two balance sheet items only, such as inventories and accounts receivable, notwithstanding the fact that such restriction calls for qualification, does not constitute sufficient reason for ex-

cluding the engagement from the class of balance sheet audits.

3. *Cash Audits.*

A cash audit comprehends verification of all receipts and disbursements for which an accounting should have been made during a period, of the accuracy of the cash records, and of the balance at the end of the period, together with the preparation of a report, with or without a certificate.

4. *General Examinations.*

A general examination covers a period, and consists of verification of assets, liabilities, capital, and surplus, as of a given date, an analytical review of income, expenses, and miscellaneous profits and losses for a period ended on that date, and the preparation of a report containing a balance sheet and a statement of income and profit and loss, with or without a certificate.

A general examination is distinguished from a general audit by omission to verify the cash receipts and disbursements, and by verifying the operating accounts through analytical study and investigation rather than by a general audit of the transactions. It is distinguished from a balance sheet audit, in the more extensive review of the operations as such, rather than as an incident to the verification of assets and liabilities.

The object of this service is to determine that there is no over-statement of net assets, or of net profits; not to determine fiduciary integrity. While, because of somewhat extensive consideration of the operating accounts, there is more opportunity than in a balance sheet audit of detecting any existing internal fraud, the service may not be relied upon in that respect. Any restriction upon the verification of one or two balance sheet items only,

such as inventories and accounts receivable, while calling for qualification of such items, does not remove the engagement from the class of general examinations.

When arising in connection with the proposed issuance of securities, mergers, consolidations, or purchases and sales of companies and properties, this type of engagement, in order to satisfy the requirements of financial agencies involved, as to condition, earning power and management, calls for a report in which particular attention is given to classification in statements and to appropriate information in the comments. The report contains, frequently, a balance sheet giving effect to the proposed financing.

While a general examination usually covers both financial condition and operations, occasionally it may be confined to such verification of income, expenses, miscellaneous profits and losses, and related balance sheet accounts, as may be necessary to determine that there has been no over-statement of net profits. In a report on an examination of this character, the statement of income and profit and loss may be certified, but a balance sheet, if submitted, should be shown as having been prepared from the books without verification.

Following Mr. Wildman's report there was discussion as to various features of the service classification. The binding of reports was discussed also, various opinions being expressed as to the merits of top-binding as opposed to side-binding. Some time was devoted to the content of reports, combination of presentation and comments, and the inclusion of operating statistics and ratios and graphic charts.

It was inevitable that a number of weaknesses would be found in the original draft of the service classification, and some

difficulties experienced in its application. Such is the case with any innovation. It was not expected that the pioneer attempt to define and differentiate the many classes of service which members of the accountancy profession have developed gradually during the course of its growth, would be perfect. The basic idea is sound, however. There is at present a great need for common understanding on the part of all concerned with accountants' services, as to just what accountants are prepared to offer; what

they undertake to do; how far their responsibility extends in individual cases. It is earnestly to be hoped that the time is not far distant when an authoritative medium will assume the task of making an official pronouncement on these matters. It is our modest desire that our efforts in this direction, although undertaken for our own guidance, may be of some use in the common cause—progress towards greater usefulness of accountants to business generally.

Some Observations on Reports

By H. L. WILSON, *Technical Procedure Department*

THE effectiveness of accountants' services depends so much upon the usefulness of their reports that no pains should be spared to make the reports clear, informative, and technically correct.

The following discussion dwells upon a few of the problems which are frequently encountered in the preparation of reports, as indicated by the review of a large number of reports recently rendered. The discussion will be taken up under the following headings: Presentation, Comments, Certificate, and Balance Sheet. The subject of profit & loss statements is not dealt with in this article.

Presentation

If the report is addressed to the concern whose accounts have been examined, the presentation need not state, "We have made a general audit (or whatever the service classification may be) of the accounts of the _____ Company," but should state, "We have made a general audit of your accounts." This is one of the few cases in which the use of the personal pronoun is appropriate in reports. In most other instances the tone of the report is more dignified if an impersonal point of view is maintained.

In cases where all or nearly all the com-

ments constitute qualifications, or are otherwise of a vital character, it is desirable to combine them with the presentation. The same practice should be followed when the comments are very brief. In combining the presentation and the comments it is necessary to give consideration to the introductory wording of the comments. The matter might well be handled thus:

We have made a general audit of your accounts, etc., etc.

[Here follows the description of statements.]

The results of the audit are further reported in the following comments:

[Here follow the comments.]

Yours truly,

If it is desirable to give a certificate, the certificate may be the final paragraph and may be worded somewhat as follows: "*We Hereby Certify* that, subject to the foregoing qualifications, in our opinion the accompanying Balance Sheet as of December 31, 1925, is correct."

In case the auditor has written up the books and at the same time has verified the accuracy of the original data, the presentation should clearly indicate the scope of his work. In reports where such service has been rendered, a number of in-