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I believe it fair to begin by summarizing George Catlett's paper as an affirmation of the conventional wisdom of the accounting profession. Adherence to the standards of a profession must always be seen by responsible citizens as admirable, and therefore criticism is difficult. In this regard, I will not present esoteric criticism that sometimes characterizes the remarks of teachers in situations such as this, nor will I dwell at length on selected statements in the paper. However, if you will indulge me, I wish to respond to one statement because it sets a tone for the paper and for the conventional wisdom of the profession which I would like to see changed. Under the heading "Representations by Clients," the following statement can be found: "[Auditors'] . . . responsibilities do not include infallibility or clairvoyance."

"Responsibilities" of CPAs

In this statement, as well as in many other parts of the paper, either explicitly or implicitly, Catlett suggests that the detection of fraud could become a "responsibility" and an onerous one at that. Presently it is reasonably clear, at least to accounting practitioners and students, that detection of fraud is not an objective of the ordinary examination of financial statements. However, should this objective be undertaken by CPAs, it would not necessarily constitute a new "responsibility." Should such an objective be assumed, it seems likely that it would result from a demand for service either directly from clients or indirectly from clients through a governmental or other agency charged to represent the public. Further, I might add, that assumption of such a "responsibility" should carry with it appropriate remuneration.

I am suggesting that the services or functions of a profession evolve over time and the nature of these services is dictated largely by customers who demand services and are willing to pay for them. Finally, I am also suggesting that the accounting profession should feel flattered and privileged to be asked to extend its services to a desirous public. This is, of course, a simplification of the rather complex problem of attesting to the material absence of fraud in the operations of an entity. To clarify my position, however, I would like to take up several specific topics included in the subject paper and attempt to relate them to this potential extension of the attest function.

Nature of Fraud

The paper outlines the nature of fraud in a manner that should be satisfying to most accountants. Examples of various types of fraud are listed and even these examples appear to be inclusive of the vast majority of frauds that are perpetrated. However, the paper dwells at length on cases of fraud which are concealed through collusion and tends to ignore defalcation and embezzlement by individuals. Catlett states that ". . . major cases usually include collusion among officers and/or employees, or collusion with outside persons." CPA firms certainly should be able to support a statement such as this one. I cannot, but I do know that there are many individuals now in prison who were convicted of embezzlement and who did not collude with anyone. Many of you probably will remember the study of defalcators published over 20 years ago in *The Journal of Accountancy*. The study by Donald Cressey centered on convicted defalcators incarcerated at Illinois State Prison at Joliet. Cressey's purpose was to determine the causes of defalcations. He generalized about the process of defalcation in the following way:

> Trusted persons become trust violators when: (1) they conceive of themselves as having a financial problem which is non-sharable; (2) have the knowledge or awareness that this problem can be secretly resolved by violation of the position of financial trust; and (3) are able to apply to their own conduct in that situation a verbalization which enables them to adjust their conceptions of themselves as trusted persons with their conceptions of themselves as users of the entrusted funds or property. Unless there is movement through this sequence, a trusted person does not become a violator.[1]

This study along with other studies by students of Dr. Cressey have indicated that some types of fraud do not include collusion. If an auditor were to attest to the material absence of fraud, he should consider this type of fraud as well as such misrepresentations by management as over- or under-statement of assets and liabilities and irregular and/or deceitful transactions. Presently, auditors have an excellent opportunity to uncover an individual defalcation through the review and evaluation of internal control. All pronouncements on the nature of internal control emphasize division of duties and responsibilities in a manner that prevents errors and defalcations unless collusion exists. If most perpetrators (at least those who are caught and convicted) have nonsharable problems and perpetrate embezzlements with no collusive help, the auditor should be able to discern weaknesses in the control system which could allow for the existence of such fraud with the use of current internal control evaluation standards and procedures.

Audit Objectives

Apparently, some frauds involve collusive arrangements, but some do not. It would seem that all should be included in any definition of fraud if a stance is taken on the subject of attesting to the material absence of fraud. However, a more important consideration to this discussion concerns objectives of audits. Historically, these objectives have changed. Brown suggests that the detection of fraud was recognized as a major audit objective until at least 1940.[2] He also indicates that beginning around the turn of the century fairness began to overshadow detection of fraud as a stated audit objective, and that detection of fraud seemed to disappear as a stated audit objective around 1940 due largely to the effect on the profession of the McKesson & Robbins case. Perhaps the discussion of the auditor's responsibility for the detection of fraud has not yet diminished because it was a stated audit objective for over 400 years and was removed as an objective by the profession rather than by a change in demand of clients of accounting firms. A solicitous consuming public could reinstate it. If this were to happen, the terms might be more advantageous for CPAs than they were during the period previous to the McKesson & Robbins case.

The detection of fraud as an audit objective might resurface as a part of the ordinary examination of financial statements or as a special examination of financial statements. Recently there has been much more interest in attestation of representations other than those which appear in historical financial statements. Forecasts and interim financial statements are two possible extensions of the attest function that are of current interest to the profession.

Whether the potential extension of the auditor's opinion is forecasts, interim financial statements, or detection of fraud, history indicates that the process will evolve slowly over time. Any extension probably will not result from a sudden pronouncement of the AICPA; instead, any such pronouncement will follow rather widespread practice in the field. Should detection of fraud again become a stated audit objective, either as a part of the ordinary examination of financial statements or through a demand for special reports asserting the absence of fraud, auditing standards must be judged for their appropriateness to the task.

Auditing Standards

Current general and field work standards seem to apply equally well to audits of financial statements and to audits designed to detect the existence of fraud. As mentioned earlier, the requirement for review and evaluation of internal control should ferret out all but the most insignificant embezzlement or defalcation perpetrated by a lone individual. The search for other types of fraud seems to be covered by the third standard of field work which requires "sufficient competent evidential matter." That standard goes on to indicate that this evidence should be obtained "through inspection, observation, inquiries, and confirmations." All of the types of fraud that result from situations other than "nonsharable problems" are transaction based. Purchases, sales, cash receipts, and cash disbursements are recorded and result in balances that appear in accounts. If the balances are incorrect due to fraud, evidence of that fraud should be available. This evidence may not always be conclusive, as sometimes seems to be true in the ordinary examination of financial statements. Nevertheless, some evidence will exist.

Because accounting data are transaction based, evidence theory indicates that auditors should corroborate client representations by obtaining information from the other party to the transaction or a third independent party such as a bank. Evidence is gathered by auditors in the field by applying this theory through the use of confirmations (a direct means) and such things as examination of invoices and cancelled checks (an indirect means). In summary, auditing standards seem broad enough to encompass audits for the purpose of detection of fraud.

In most of the fraud cases that are covered in the literature there are problems of interpretation of auditing standards, and in a few cases, apparent violations of them. As Mr. Catlett suggests, standards must be distinguished from procedures and I would suggest that it is procedures used in applying standards that might have to be changed should fraud detection become an objective of either a special examination or the ordinary examination of financial statements.

Auditing Procedures

The changes that should occur in audit procedures are really changes that should occur whether or not fraud detection becomes an objective of the ordinary examination. To discover any characteristic of a population of data, sampling techniques can be used. Discovery sampling, for example, seems particularly appropriate to investigation of potential frauds. Discovery sampling is not particularly helpful in situations where fraudulent transactions or behavior constitute an extremely minor percent of the transactions or behavior experienced in an organization. However, if fraud is material, such techniques could be helpful.

Scientific sampling currently is very helpful in the ordinary examination of financial statements. The characteristics of interest are different, but the purpose is identical: to discover characteristics and assess their importance. It is difficult to assess the degree to which statistical sampling is utilized by auditors, but it seems clear from the literature that it is far more reliable than judgment sampling techniques. Should detection of fraud become an objective of the auditor's examination, scientific sampling certainly would have to be used in order to assess the risk taken in attesting to the absence of material fraud. Also, an auditor should be interested in assessing the risk he is now taking in his opinion on financial statements for an ordinary examination where fraud is explicitly denied as an objective.

One additional example of an audit procedure that might change should fraud again become an audit objective is confirmation. It is my understanding that negative confirmation requests are still quite prevalent in spite of the fact that when an auditor does not receive a reply from a request, he has no basis for determining whether the amount to be confirmed is correct or the respondent is nonexistent, uninterested, or unresponsive. In an audit of accounts receivable, if confirmation requests were sent and the objective were to determine whether the accounts receivable were fraudulently stated, I do not believe that many auditors would want to rely on the use of negative confirmations. Instead, positive confirmations would be utilized with careful and extensive followup. Again, I would suggest that such procedure would be appropriate in the ordinary examination where the objective is not detection of fraud; however, it becomes much more important when the objective is detection of fraud.

Professional Audit Service

Earlier, it was suggested that the use of the term "responsibility" perhaps was inappropriate. Instead it was suggested that demands for CPAs' services should be treated as opportunities and privileges to serve society. When such requests are made, they represent recognition by society that CPAs have the competence and the integrity to perform the services requested. Competence often is brought into arguments against extension of the attest function to other areas. In such arguments it is suggested that the competence of CPAs lies in their abilities as accountants and that to attest anything or offer a service that is outside of the field that has been known traditionally as accounting would be to engage in services beyond their abilities and that therefore the public might lose confidence. This, of course, could happen; however, in my opinion CPAs will not seek out engagements in which they must offer a service that they have not offered previously. Rather, society will ask CPAs to provide the new service. This has happened in many instances over the years to the extent that management services departments of CPA firms engage in salary surveys, executive search and other activities that cannot be considered, even remotely, as traditional accounting services. Thus far, no consequent loss of public confidence has occurred.

Although I am not a practitioner, I think there is one change that should be made in the practice of public accounting, should requests for extensions of the attest function and other services be made by the public. In almost every profession, some allowance is made in the fee structure for the relative risk involved. Delicate surgical operations are more expensive than routine low-risk surgical operations. With the possible exception of some securities registrations, CPAs apparently have not built into their billing structures any allowance for risk that might be present in a given engagement. Should CPAs be asked to attest to the absence or presence of material fraud, it would seem wise to adjust billing methods to allow for risks being undertaken. Again, there is a parallel to attestation of financial statements. Given current litigation against accountants, it would seem appropriate for CPAs to assess risk in each ordinary engagement and adjust the fee according to the estimate of the risk to be undertaken.

Conclusion

Services or functions of any profession evolve over time and should be seen as opportunities or privileges. At the same time, professionals should assess the value of their services and the risks that may be involved and bill clients accordingly. Furthermore, historically, audit examinations with some stated objective have been undertaken before standards were developed. As indicated previously, Brown asserted in his article that audits occurred prior to the year 1500 and were carried on for hundreds of years before auditing standards were developed. A more recent example is that of attesting to some aspects of forecasts. Such services have been performed and are being performed now by CPAs without any explicit standards. Therefore, I think it is unreasonable to assume that standards should be developed before examinations with the stated objective of detection of fraud can be undertaken.

Finally, there is one important suggestion that comes from this paper. Mr. Catlett made assertions about the nature of fraud which can be substantiated through research. If there is client interest in attestation to the absence or existence of material fraud, research should be undertaken in the area. Almost all CPA firms maintain files with experiences catalogued in many different ways. As a first step, it would be interesting to examine the files of CPA firms cataloging all types of fraud that have been discovered either during the course of an examination or afterward. A classification system for this examination might include type of fraud, method of concealment, industry, client size, and the circumstances surrounding the discovery of the fraud. Only after extensive research of this type can the profession properly assess the likelihood of discovery of fraud and the risk the CPA is taking when he attests to the absence of it.

Catlett's paper concludes with the following statement: ". . . the accounting profession must not permit itself to be destroyed by assuming responsibilities or accepting a role that cannot be successfuly fulfilled." I would add to that statement that the accounting profession must not permit itself to be destroyed by refusing to provide requested services to society. Destruction in this latter case will be much slower but nonetheless definite.

Footnotes

1. Donald R. Cressey, "Why Do Trusted Persons Commit Fraud? A Social-Psychological Study of Defalcators," *The Journal of Accountancy,* November 1951, pp. 577-578.
2. R. Gene Brown, "Changing Audit Objectives and Techniques," *The Accounting Review,* October 1962, pp. 696-703.