

DISCUSSION DOCUMENT SCASS No. 1

One of the purposes of this society is to stimulate discussion upon current accounting issues, and hence to broaden the minds of its members. Therefore we have commissioned a report by Sir Tinlee Able, one of the foremost experts in his field (Parapsychotics and nuclear accidents) on certain issues which have been the subject of much confusion in the past.

We present his full report for your scrutiny and comment.

Recent developments in the field of mathematics seem to cast a worrying light on current auditing practice. The following matters should be given the fullest consideration at your nearest convenience.

CHAOS THEORY

Given any system with inputs and outputs, it has been observed that small changes in inputs may give rise to unpredictable outputs.

For example, the effect on the financial director of a small change to an audit report – commonly known as a “qualification” – can result in an unexpected state – known as “apoplexy”, easily recognizable by the transition from utter outrage to incoherent vegetation. Clearly the benefits of being able to predict such behaviour are considerable.

Whilst such system behaviour may be modelled using electronic circuits, it is suggested that an approach using computers is unwieldy. The preferred approach today is to sit quietly playing with two paperclips, a small watch battery and a cold cup of coffee until either the ambulance arrives or you are over budget.

CATASTROPHE THEORY

A client’s accounting system may be described as a “black box” (ie. a mechanism of whose internal workings we may be totally ignorant) with an input and a series of outputs.

Thus the input of an auditor into such systems results in the output of a slightly changed auditor (things to watch for are a docile, dazed disposition, dark rings round the eyes and a disinclination to do anything but burble quietly in a corner whilst clutching a soggy audit manual).

There are however certain critical inputs whose entry into the system causes very large and often bizarre changes in the output. Such an example might be an auditor entering the system and emerging as an accountant, or worse, a manager. Fortunately we can model the effects of the critical inputs – commonly used yardsticks being GCC, PE1, PE2 and hence we can predict the outputs and make allowances accordingly.

HEISENBERG’S UNCERTAINTY PRINCIPLE

This anomaly causes the gravest of concern to the members of the committee and deserves fuller exposition than the current climate allows.

Essentially, the process of measurement of the size of an item alters the characteristics of that item, and vice versa.

Thus the act of determining the location of an item in the financial statements renders the determination of the size of that item extremely difficult. Similarly, the discovery of the size of an item causes great uncertainty as to the location of that item.

Current methods of dealing with this problem involve the use of “materiality” to limit the accuracy with which the item’s location or size is determined.

The risk of the item being either misplaced or misstated can then be controlled. The extent to which it is not controlled is known as audit risk (i.e. it is the risk that an item is misstated, misplaced and that the auditor doesn’t know where or what it is anyhow).

Historically, these three areas have been considered separately, but a new development is to weave them together

$$CT + H'sUP = C$$

into what is challengingly called the “Audit Risk Model”; Or, in plain English, Chaos plus Uncertainty equals Catastrophe.

Interpretation is then straightforward. The more chaotic the audit and the less certain the location and size of items in the financial statements (limited by materiality) then the more likely it is that an auditor will emerge successfully from the black box as an accountant. The implications of this are tremendous.

By limiting exposure to accounting systems, we can decrease chaos and uncertainty!!!

This is of course in line with the second Law of Thermodynamics which states that entropy increases – this means that chaos and uncertainty are a natural by-product of working.

In each of the above situations there is scope for the raising of current auditing practice and comment is invited upon them. Remarks on a postage stamp to the Head of State, Rio de Janeiro primary school for recalcitrant auditors.

(Sir Tinlee Able’s report on the Chernobyl accident was met with much acclaim, and quickly censored by Soviet authorities.)