

1927

Examination [1927]

Virginia State Board of Accountancy

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EXAMINATION
VIRGINIA STATE BOARD OF
ACCOUNTANCY

RICHMOND, VIRGINIA
OCTOBER 24, 25 AND 26, 1927

PRICE 25 CENTS PER COPY.

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EXAMINATION VIRGINIA STATE BOARD
OF ACCOUNTANCY

COMMERCIAL LAW

OCTOBER 24, 1927—9:00 A.M. TO 1:00 P. M.

Answer all Twelve Questions

Designate Answers According to Numbered Questions

- (1) A brings an action at law against B and proves at the trial that he (A) loaned C \$500.00 and that B verbally promised to repay the same. What judgment should the court enter and why?
- (2) Williams in Baltimore wires Robins in Richmond, Va., as follows: "Offer for shipment today 100 Barrels high grade apples at \$5.00 per barrel F.O.B. Baltimore." Robins writes Williams as follows, "Your offer received and accepted. Ship via R. F. and P. R. R." Prior to receipt of this letter Williams wires Robins, "Our offer today withdrawn, apples sold to others." Robins sues Williams for breach of contract. Judgment for whom and why?
- (3) (a) Doe, a street car conductor throws Roe violently from the street car because Roe refused to pay his fare claiming he had already paid it. Roe sues the Street Car Company and proves he had actually paid his fare and that he was injured by his fall. Judgment for whom and why?
(b) Later on the above trip Doe, the conductor, sees Johnson on the sidewalk. Johnson and Doe were on bad terms so Doe jumps from his car and gives Johnson a sound beating injuring him severely. Johnson sues the Street Car Company. Judgment for whom and why?
- (4) J. R. Long let a contract to the A. B. C. Corporation for the erection of a warehouse. During the construction of the building the A. B. C. Corporation became unable to pay its sub-contractors. The sub-contractors were unwilling to perform their contracts unless they were assured of their pay. Under these circumstances Long sent a circular letter to all the sub-contractors to the effect that he would pay their bills against the A. B. C. Corporation. The sub-contractors, relying on this letter, but without notifying Long completed their contracts and sent him their bills. These bills amounted to more than the contract price of the building. Is Long liable for such excess? Give your reasons.
- (5) (a) What negotiable instrument, if any, must be protested upon dishonor in order to hold persons secondarily liable?
(b) When, if ever, is the drawee Bank liable to the payee of a check?
- (6) A negotiable note is made by Curran payable to Putnam, and is indorsed before delivery by Ransom for the accommodation of Putnam. Putnam then indorses the note to the Mechanic's Bank. What is the liability of Ransom to (a) the Bank; and (b) Putnam?

- (7) Paul, Largen and Martin were partners in a mercantile business which became insolvent and a receiver was appointed. The partnership assets amounted to \$1,000.00, its liabilities to \$2,500.00, Paul owned assets valued at \$2,000.00 and owed personal debts amounting to \$1,500.00; Largen owed personal debts amounting to \$350.00 and had nothing; Martin owned assets valued at \$1,800.00 and owed personal debts amounting to \$1,500.00. How should the court distribute the assets upon the indebtedness?
- (8) A made a will in 1904 in which he left legacies to his three children then living, as follows:

B.....	\$40,000
C.....	50,000
D.....	60,000
Total.....	\$150,000

- In 1905 another child named E was born, but no change was made in the will. A's wife died in 1920, and in 1927 A himself died. A's net estate, after the payment of all debts, executor's commission, funeral and administrative expenses, etc., amounted to \$240,000, consisting of cash and marketable securities. How much will each of the children receive, if anything?
- (9) (a) Where the capital stock of a corporation just organized has a par value of \$100.00 per share and 1,000 shares are sold at \$75.00 per share, (a) what entry would you make to take care of this difference? and (b) what, if any, is the liability on the subscribers for this difference?
- (10) (a) Within what time can preferred stock be made redeemable by the charter of the corporation?
 (b) Name two methods by which a corporation can change the location of its principal office named in its charter.
 (c) What is the remedy in Virginia of an aggrieved dissenting stockholder in the event of the merger of the corporation in which he owns stock, with another engaged in a similar business?
- (11) A makes an application to the Bank for a \$500 loan and to induce same makes a willful fraudulent written statement as to his financial condition. Being unable to pay the note when due A becomes a voluntary Bankrupt listing many creditors. Is A entitled to a discharge (a) from the Bank's debt and (b) from all of his other debts?
- (12) What is the Statute of Limitations in Virginia on the following:
 (a) A sealed instrument
 (b) A negotiable note
 (c) An open account.

PRACTICAL ACCOUNTING

PART 1

OCTOBER 24, 1927, 2:00 P. M. to 6:00 P. M. (FOR PROBLEMS I, II AND III)

PROBLEM 1

The H. K. Jones Company is a small corporation manufacturing a high-gloss varnish under a patented formula.

Its balance sheet December 31, 1926, is as follows:

Cash.....	\$ 500.00	Accounts payable.....	\$ 3,000.00
Accounts Receivable.....	2,000.00	Bills payable.....	4,000.00
Materials.....	2,500.00	Capital Stock.....	10,000.00
Finished product.....	2,000.00	Surplus.....	5,000.00
Formula.....	15,000.00		
	<hr/>		<hr/>
	\$ 22,000.00		\$ 22,000.00

The stock is in \$100 shares and is owned as follows:

H. K. Jones.....	90 shares
Mrs. H. K. Jones (wife).....	5 shares
Willie Jones (son).....	5 shares
	<hr/>
	100 shares

As creditors are pressing and Jones sees he cannot continue without further liquid capital he takes the matter up with Allen Brown who has some idle money and makes him the following proposition: "Give me personally \$2,500 in cash; pay off the notes payable of the business and pay \$2,000 into the corporation treasury—for this I'll transfer to you 40 of my shares in the business and have issued to you 20 shares of new stock, thus giving you a one-half interest in it." Brown accepts.

1. Make a balance sheet after completion of above.
2. Give the profit or loss of Jones on the deal presuming balance sheet figures represent actual value.

PRACTICAL ACCOUNTING

PART 1

PROBLEM 2

On September 1, 1926.—The Mayodan Mills, makers of cotton yarns, had been idle since the previous January.

September 12.—They received an offer from Excelsior Hosiery Mills to make for them 600,000 pounds cotton yarns @ 60c per pound for equal deliveries October, November, December, January, February and March.

They estimated that on the present price of cotton they could make a small profit on this basis and accepted the business making firm contract for delivery as above specified.

September 15.—To avoid buying their whole requirements now and to protect themselves on material, they purchased through their brokers in New York future contracts as follows:

4 October	(400 bales)	@	20.25	(cents per pound)
4 December	(400 bales)	@	20.50	(cents per pound)
4 March	(400 bales)	@	20.75	(cents per pound)

Cash margin put up \$500 per contract or \$6,000.

September 28.—Bought from Jennings Warehouse Company 500 bales (250,000 pounds) cotton delivered at mill @ 20.60.

October 5.—Sold four October contracts @ 21.50 and received proceeds and returned margin less commission of \$25.00 per contract.

October 25.—Sold four December contracts at 22.50 receiving proceeds and returned margin, less commission.

December 3.—Bought of Jennings Warehouse Company 500 bales (250,000 pounds) @ 21.00 delivered.

December 31.—This being the end of the operating year they want the books closed. The superintendents reports 600 bales opened and used to date. The company concludes to hold its March future contracts till later.

March futures closed December 31 @ 20.00 (Cents per pound)
Spot cotton quoted at Jennings Warehouse at 20.00 (Cents per pound)

Make up Journal enteries for above transaction and post showing ledger accounts.

Close above ledger accounts as at December 31 showing balances brought down or into what accounts closed.

NOTE (1)—Bales to be figured at 500 pounds throughout.

NOTE (2)—No entries with reference to delivery of finished product need be made.

PRACTICAL ACCOUNTING

PART 1

PROBLEM III

The Brown Investment Company was formed in 1898 to acquire the capital stock of the Brown Carriage & Buggy Company, a very old and prosperous business. The stock in the holding company being taken by the holders of Carriage & Buggy Co., in proportion to their holdings in Carriage & Buggy Company. From 1898 to 1910 heavy dividends both out of old surplus and yearly earnings were paid to the holding Company which invested them in various liquid securities. In 1910—\$10,000.00 par value new stock of the Brown Carriage Company was issued and sold at par to certain employees. Up to 1920 profits were made and good dividends paid, but since, losses have been heavier each year, and at the close of the year 1925 it was decided to close up and liquidate the Carriage & Buggy Company.

The Balance Sheets of the two companies on December 31, 1925, as made by themselves are as follows:

BROWN CARRIAGE & BUGGY COMPANY

ASSETS	LIABILITIES
Power Plant—Land, Bldgs., & Machinery.....\$ 50 000 00	Brown Investment Co.....\$ 105 000 00
Mfg. Plant—Land, Bldgs. & Machinery..... 100 000 00	Capital Stock..... 110 000 00
Various Cut-over Timber Lands..... 5 00	Reserve for Depreciation
Inventories—Finished Vehicles..... 5 000 00	Power plant..... 20 000 00
Inventories—Material & Supplies..... 10 000 00	Mfg. plant..... 65 000 00
Inventories—Patterns, Designs, etc..... 5 000 00	
Inventories—Show-room Vehicles..... 5 000 00	
Accounts and notes..... 20 000 00	
Cash..... 1 000 00	
Deficit..... 103 995 00	
\$ 300 000 00	\$ 300 000 00

BROWN INVESTMENT COMPANY

Cash.....\$ 10 000 00	Capital Stock.....\$ 100 000 00
Bonds & Liquid Securities.... 500 000 00	Surplus..... 510 000 00
Stock in Brown Carriage Company (par)..... 100 000 00	
\$ 610 000 00	\$ 610 000 00

At the end of 1926 the liquidating committee reports the following transactions during the year with reference to Brown Carriage & Buggy Company:

(1) Leased the Power Plant to the City of Brownville for 15 years at an annual rental of \$3,000.00, at the end of which time the city is to pay \$10,000.00 additional and the property is to be deeded to the city. Received 1926 Rent.

(2) Gave the Manufacturing Plant Buildings and Machinery to a wrecking company in consideration of moving them from the land,—Had Land appraised by three real estate men—average valuation \$20,000.00—Holding for offers.—

(3) Sold Finished & Show Room Vehicles at Auction for \$500.00—Sold Materials & Supplies for \$6,000.00—Patterns and Designs—Worthless—No sales—

(4) Discovered among papers, autograph letter to founder of company from Andrew Jackson, ordering a carriage,—Sold letter to museum for \$1,000.00.

(5) Collected accounts and notes \$10,000.00; Consider \$3,000.00 of remainder good.

(6) Bought in \$10,000.00 capital stock owned by employees at par as per agreement at time of decision to liquidate.

(7) Turned over to Brown Investment Company on account \$10,000.00.

(8) Have nothing so far to report as to cut-over timber lands.

Assuming that the Brown Investment Company during 1926 had Income from Interest \$30,000.00 and paid expenses \$12,000.00, you will make up the following as of December 31, 1926:

(a) Balance Sheet of Brown Carriage & Buggy Company.

(b) Balance Sheet of Brown Investment Company.

PRACTICAL ACCOUNTING

PART 2

OCTOBER 25, 1927—9 A. M. TO 1. P. M.

PROBLEM IV

The Triangle Fertilizer Company manufactures and sells chemical or commercial fertilizers for staple crops. As one of the principal ingredients of chemical fertilizer is acid phosphate, this company also manufactures this commodity, part of which goes into its own fertilizers and part is sold to other manufacturers.

The accounting system is so arranged that the cost of producing both fertilizer and acid phosphate may be obtained from the books. To this end three ledgers are kept—viz:

- (1) Acid Phosphate Plant Ledger—In this is kept all accounts relating to the production of acid phosphate.
- (2) Fertilizer Plant Ledger—In this is kept all accounts relating to the production of Fertilizer.
- (3) General Ledger—In this are kept all the asset and liability accounts (except Inventories), all the operating accounts not specifically assigned to plant ledgers and the balances on all reserves. The plant ledgers are represented by single accounts on the general ledger, which accounts serve as controls of the plant ledgers.

On January 1, 1927, you are requested to make up for this company as of December 31, 1926, the following:

- (1) Statement of Assets and Liabilities as at December 31, 1926.
- (2) Operating Statement for year 1926.
- (3) Memorandum of average cost for period of producing
 - (a) One ton acid phosphate ready for use or sale.
 - (b) One ton Fertilizer ready for sale.

You have available the trial balances of the three ledgers as of December 31, 1926, statement of Inventories at December 31, 1926, and sundry data as to methods and practices peculiar to this company and this industry. You will accept these methods in your work.

The above available information is given herewith; from it you will prepare the statements requested.

GENERAL LEDGER

<p>Acid Phosphate Plant—</p> <p style="padding-left: 20px;">Bldgs.....\$ 20 000 00</p> <p style="padding-left: 20px;">Machinery..... 54 000 00</p> <p>Fertilizer Plant—Bldgs..... 25 000 00</p> <p style="padding-left: 20px;">Machinery..... 41 000 00</p> <p>Plant Lands..... 10 000 00</p> <p>Furniture and Fixtures..... 4 000 00</p> <p>Cash..... 10 000 00</p> <p>Accounts Receivable..... 80 000 00</p> <p>Selling Expense..... 20 000 00</p> <p>General and Administrative Exp..... 12 000 00</p> <p>Supt. of Manufacturing Salary..... 4 000 00</p> <p>Factory Office Expense..... 6 000 00</p> <p>General Office Expense..... 10 000 00</p> <p>Interest Paid..... 8 000 00</p> <p>Acid Phos. plant Ledger..... 71 100 00</p> <p>Fertilizer Plant Ledger..... 239 050 00</p> <hr style="width: 100%;"/> <p style="text-align: right;">\$ 614 150 00</p>	<p>Accounts Payable.....\$ 20 000 00</p> <p>Notes Payable..... 100 000 00</p> <p>Sales—Fertilizer..... 300 000 00</p> <p>Sales Acid Phosphate..... 17 000 00</p> <p>Reserves for Depreciation:</p> <p style="padding-left: 20px;">Acid Phos. Bldgs. (1-1-26).. 2 000 00</p> <p style="padding-left: 20px;">Acid Phos. Machy. (1-1-26) 14 000 00</p> <p style="padding-left: 20px;">Fertilizer Plant (1-1-26)..... 5 000 00</p> <p style="padding-left: 20px;">Fertz. Machy (1-1-26)..... 6 000 00</p> <p style="padding-left: 20px;">Furniture & Fixt. (1-1-26)..... 1 000 00</p> <p>Reserves for Repairs:</p> <p style="padding-left: 20px;">On Acid Phos. plant (1-1-26) 8 000 00</p> <p style="padding-left: 20px;">On Fertz. plant (1-1-26)..... 2 000 00</p> <p>Capital Stock..... 100 000 00</p> <p>Surplus..... 39 150 00</p> <hr style="width: 100%;"/> <p style="text-align: right;">\$ 614 150 00</p>
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SUNDRY DATA

- (1) The two plants are under one superintendent and all details of payroll, formulating, etc. are handled in one factory office situated between the plants, otherwise all operations are separate. The company considers that 34% of the Superintendent and Factory Office burden is allocable to Acid Phosphate, the remainder to Fertilizers.
- (2) In the Fertilizer plant the product goes through two successive processes; first, the raw material is milled and stocked in piles, second, the stocked material is screened and bagged. Some time may elapse between the operations, the second being applied only when goods are to be shipped out.
- (3) In order to equalize repair charges over the years 30 cents per ton is set up as a Reserve for Repairs in the Acid Phosphate Plant for each ton made and considered as an item of cost. Actual expenditures for repairs are to be charged to the Reserve so created. The Reserve entry is to be made at the end of each year.
The same method is used in the Fertilizer plant, the rate being 10 cents for each ton put through each process or 10 cents per process per ton.
- (4) Depreciation rates are:

Acid Phosphate Buildings.....	3%
Acid Phosphate Machinery.....	10%
Fertilizer Buildings.....	5%
Fertilizer Machinery.....	5%
Furniture & Fixtures.....	10%
- (5) In case it becomes necessary to prorate any charge or burden between the two processes in the Fertilizer plant, it is to be done on tons per process basis; the charge per ton being considered equal for each process.
- (6) General and Administrative Expense and General Office Expense will not in this problem be considered as elements of production.

THEORY OF ACCOUNTS

OCTOBER 25, 1927—2 P. M. TO 6 P. M.

Answer all Questions

Do Not Repeat Questions But Designate Them By Numbers And Letters

1.
 - (a) Distinguish between Repairs and Renewals and Additions.
 - (b) Under correct accounting procedure to what accounts should each be charged on the books?
 - (c) Has incorrect accounting in respect of any of the foregoing any effect upon the accuracy of the depreciation rate or the adequacy of the depreciation reserve? If so, explain fully.
2. State the position on the Balance Sheet at December 31, 1926 of the following items and your reasons for such classification:
 - (a) Notes Receivable Discounted
 - (b) Sinking Fund Reserve (all bonds having been retired)
 - (c) Deferred Operating Expense
 - (d) Premium on Capital Stock sold for cash
 - (e) Serial Note issue maturing September 30, 1927, 1928 and 1929.
 - (f) Unamortized bond discount and expense
 - (g) Investment in stock of subsidiary corporations
 - (h) Funds for redemption of bonds
 - (i) Unexpired insurance premiums (policies expire three years from September 30, 1926)
 - (j) Claim vs. U. S. Government for refund of U. S. Income and excess Profits Taxes and Interest.
3. A corporation insures the life of one of its officers on the straight life plan, and the policy has a cash surrender value at the end of the third year. (a) What entries should be made during the first four years? (b) If the officer dies at the end of the fifth year, what entry or entries should be made on receipt of the principal from the insurance company?
4. Is it proper under any circumstances to enter on the books Fixed Assets of a going concern at more than actual cost? Explain fully
5. A company uses its own labor and materials in making extensive additions to its plant at a cost much less than the contract price of outside contractors. What objection, if any, do you see to charging the improvement with the contract price and crediting Profit and Loss Account or Surplus with the difference?
6. If a corporation purchases its own capital stock at more or less than par, (a) How would you handle the transaction on the books? (b) On the Federal Tax Return?
7. Smith, Jones and Brown form a partnership to which Smith contributes \$50,000.00, Jones contributes \$40,000.00 and Brown agrees to manage the business for a yearly salary of \$6,000.00. Partners are to receive interest at rate of 6% on capital invested and profits or losses are to be shared on a basis of 5, 4 and 1 re-

- spectively. At the end of two years the partnership liquidates and the net assets realize \$30,000.00. No interest on capital invested has been credited to the partners' accounts and the partnership owes Brown six months' salary. Prepare statements showing final distribution to each partner.
8. How should the following items be handled at time of taking inventory?
 - (a) Goods ordered but not yet received.
 - (b) Goods received but not yet entered on the books.
 - (c) Goods held on consignment for account of a principal.
 - (d) Goods out on consignment for sale by an agent.
 - (e) Goods sold for future delivery.
 9. Define the following:
 - (a) Corpus
 - (b) Income
 - (c) Life Tenant
 - (d) Remainderman
 - (e) General Legacy
 - (f) Specific Legacy
 - (g) Executor
 - (h) Administrator
 - (i) Devise
 - (j) Bequest
 10. What advantages, if any, accrue from the issue of no-par value stock—
 - (a) To the stockholder?
 - (b) To the issuing Corporation?
 - (c) How would you express the account on the Balance Sheet when the corporation has a
Deficit?
Surplus?

AUDITING

OCTOBER 26, 1927—9 A. M. TO 1 P. M.

Answer all Questions

Do Not Repeat Questions But Designate Them by Numbers and Letters

1. If you were engaged to make an examination of a Trust Company doing a general banking business as at a certain date would you consider it necessary to verify the revenue and expense accounts, if so, to what extent and what procedure would you follow? What exhibits and schedules would you ordinarily submit with your report covering the examination as a whole?
2. (a) What verification would you make of the accounts usually included under the heading "Fixed Properties"? Would you consider a deed to the property conclusive evidence of ownership? Explain fully.
(b) The president of a manufacturing corporation for whom you have installed a cost system makes this statement to you:
"We have just closed our books for the first six months on the Basis of the system installed by you and are surprised to note that we have not been getting the production anticipated. The units produced fall far short of our estimates, and there appears to be a deficiency in the work in process and factory material. We do not feel that the system is at fault, but fear that the results are due to our lack of understanding as to the proper handling of the accounts, or to some other cause". You are requested to make a thorough investigation of the accounts (business) and report your findings. Submit your report.
3. In making a balance sheet audit you are given by the bookkeeper statements of all creditors' accounts standing open on the books. Would you consider these satisfactory evidence as to the correct liability in respect of accounts payable? Explain fully. What would your attitude be if you found that a majority of the accounts receivable had been settled by note, but no entry had been made of the note other than a memorandum on the customers' account?
4. State the various classes of taxes levied by the Federal, State (Virginia) and local governments that you would expect to find paid in making an audit of (A) A large manufacturing corporation. (B) A merchant. Of those named by you, which require the filing of a return by the taxpayer? Would you consider a cancelled check a proper receipt for the payment of these taxes? Why?
5. Outline a system of accounts for a municipality. Show the correlation of the accounts of the various officers and provide a systematic internal check between them.
6. In an audit in which you are engaged you find that the accounts receivable and accounts payable are kept in one controlling account

which shows a debit balance of \$15,000.00. An analysis of the subsidiary ledgers reveals the following:

Accounts Receivable—Customers.....	\$ 40,000.00	
" " Officers.....	5,000.00	
Debit Balances—Creditors.....	3,000.00	
Fire Insurance Premiums paid day prior to audit.		
Invoices not entered.....	1,250.00	
Capital Stock Subscriptions not fully paid.....	10,000.00	
Accounts Payable—Creditors.....		\$ 35,000.00
Unpaid Officers' Salaries.....		\$ 7,500.00
Credit Balances—Customers.....		1,025.00
Payments Received in Advance for Shipments not yet made.....		725.00
Balance.....		15,000.00
	<hr/>	<hr/>
	\$ 59,250.00	\$ 59,250.00

What disposition would you make of these items, and how would you treat them in a balance sheet.

7. What responsibility attaches to an auditor in respect of the following:
 - (a) Inventories, as follows:
 - Merchandise—Retail Store
 - Raw Material
 - Work in Process
 - Finished Goods
 - (b) Salaries and Payrolls
 - (c) Depreciation
8. A corporation decides to make an appropriation from its surplus profits for the amount of a permanent investment in property. What in your opinion would be the proper accounting record to make thereof? Would you consider this procedure necessary, or of any advantage, in a transaction of this nature?
9. In beginning an audit you find that the time allotted you in which to render your report is limited and that an exhaustive examination is impossible in the circumstances. You are requested, however, to go as far as you can and to cover those points you consider most important. State how you would proceed with the audit and to what particular features would you direct your attention. What qualifications, if any, would you make in your report?
10. Define and state the scope of a:
 - (a) Balance Sheet Audit
 - (b) Complete Audit
 - (c) Continuous Audit
 - (d) Cash Audit