1930

North Carolina C.P.A. examination

North Carolina. State Board of Accountancy

NORTH CAROLINA C. P. A. EXAMINATION

Accounting Theory

THURSDAY, NOVEMBER 20, 1930, 2 TO 6 P. M.

Question 1:

A, B, and C were partners in an enterprise for many years. At October 31, 1930, having found a purchaser, they sold their business and retired. The books show net assets of $400,000.00 exclusive of cash (which was $30,000.00), and for such net assets, excluding cash, the partnership received $460,000.00 in cash. During the period of the partnership, which was exactly twenty years, A drew an annual salary of $10,000.00 a year; B, $12,000.00; and C, $15,000.00. Net profits, after deducting salaries, were to be shared equally. There were no withdrawals other than salaries and no additional capital invested. No interest was to be allowed on capital contributions.

It is A's contention that the proceeds of the sale of the business should be distributed according to the original capital contributions which were: A, $40,000.00; B and C, $30,000.00 each. B and C believe that the cash should be divided in accordance with the profit-and-loss-sharing ratio.

Prepare a statement showing the proper distribution between the partners.

Question 2:

Your client, a small manufacturing concern, occupies rented land and has signed a 25-year lease, which does not contain a renewal clause. On the land, he has erected a building having an estimated life of 40 years, at a cost of $15,000.00. On his books a 4% depreciation rate has been employed which fully depreciates the building at the termination of the lease.

(a) Do you believe that the depreciation rate of 4% is correct?

(b) If, at the end of the fifteenth year, the lease is canceled and a new one for 35 years is signed, would you at that time recommend any change in the depreciation rate?

(c) What depreciation rate would you have recommended at the outset, if the orgiginal lease had contained a clause giving your client the option of renewal for 25 years?

Question 3:

Your client, a dealer in automobiles, has asked your views as to the proper method of accounting to be followed in handling repossessed cars. He does not sell his receivables and is particularly anxious to know his total profit or loss on these transactions, including that arising from the disposal of the repossessed cars.

Question 4:

The Farmers' Protective Association is an organization operating in Minnesota for the purpose of keeping its members informed as to the market for their products. Each member is assessed $15.00 on December 31st of each year as his portion of the maintenance of the Association for the coming year. Following is a condensed trial balance of the Association at December 31, 1929:

Particulars	Debit	Credit
Cash	$15,463.82	
Dues receivable	22,455.00	
Inventory of supplies	1,214.16	
Furniture and fixtures, less depreciation reserve	7,246.19	
Accounts payable		$ 1,206.08
Accrued expenses		891.16
Dues billed in advance (1930 dues)		37,920.00
Surplus		6,361.93
Totals	$46,379.17	$46,379.17

An analysis of the dues receivable reveals the following:

Particulars	*Amount*
Unpaid 1929 dues, considered collectible	$ 1,545.00
1930 dues	37,920.00
	$39,465.00
1930 dues paid in advance	17,010.00
Balance, as above	$22,455.00

Prepare a balance sheet at December 31, 1929. Set forth therein the above facts in accordance with good accounting practice. Give your reasons for the method you have followed in handling dues.

Question 5:

The Orinoco Manufacturing Company had a fire that destroyed its entire plant, equipment, and inventories on July, 1, 1930.

At the date of the fire the accounts on the books relating to the above items were as follows:

Particulars	*Amount*
Building cost January 1, 1910, $95,000.00; appraised value at March 1, 1913, $120,000.00; cost of new wing to old building placed in operation March 1, 1928, $75,000.00; carried on books at value according to appraisal on September 1, 1928, of	$250,000.00
Reserve for depreciation—Building, to July 1, 1930 (correctly computed)	
On March 1, 1913, value from that date to July 1, 1930 (40-year life from 3—1—13)	$ 52,000.00
On new wing (25-year life)	7,000.00
On appreciation	4,114.00
	$ 63,114.00
Machinery, carried on the books at cost, less depreciation to July 1, 1930	$ 57,250.00
Inventory, per perpetual inventory records and cost sheets, all destroyed	$ 62,250.00

Insurance received and replacements made were as follows:

Asset	*Insurance recovered (September, 1930)*	*Reinvested 1930 (replacement completed)*
Building	$205,000.00	$210,000.00
Machinery	68,000.00	62,000.00
Inventory	50,000.00	60,000.00

What was the income subject to Federal income tax in 1930? What is the cost of each class of assets for subsequent tax purposes?

Question 6:

From the following data extracted from the audited statements of the C B C Company, determine the reason for the increase in gross profit and prepare a statement reflecting such changes:

Particulars	*Year ending June 30* 1929	1930
Sales	$329,729.40	$333,067.50
Cost of sales	237,332.70	240,252.69
Gross profit	$ 92,396.70	$ 92,814.81

Units sold in 1929 were 72,468, and in 1930, 74,015.

Question 7:

In preparing an application-of-funds statement, what treatment would you accord the following items:

(a) The depreciated value of machinery scrapped.
(b) Amortized discount on bonds charged to profit and loss.
(c) Goodwill charged off to surplus.
(d) Payment of mortgage notes due.
(e) Decrease in working capital.
(f) Loss from operations.
(g) Land acquired through issue of capital stock.

Question 8:

In the consolidation of the F and G Companies and the formation of the H Company therefrom, the stockholders of the respective companies have agreed to accept the new company's 7% cumulative preferred stock, at par, for their equities in the book values of the net assets. The equity of a stockholder of one company will thus include a share of the book values of the net assets of the other company, since each company owns stock in the other, as shown below. No-par-value common stock of the new company will be distributed among the stockholders of F and G Companies on the basis of the earning power of each company, without reduction for preferred dividends. Such earning power is to be determined by the average annual net profits for the last five years, including the proper portion of the net profits of the other company attributable to the intercompany stockholdings. For each $10.00 of average annual net profit one share of no-par common will be issued. No intangible assets are on the books of either company.

One hundred and twenty thousand shares of the $100-par-value preferred stock and one hundred thousand shares of no-par-value common stock have been authorized and as many shares as may be called for by your computation will be issued.

Pertinent data follows:

Net worth of old companies:

Particulars	*Company* *F*	*G*
Common stock ($100.00 par) shares outstanding	49,650	28,800
Common stock at paid-in value	$4,965,000.00	$2,880,000.00
Sinking fund reserve	325,000.00	
Earned surplus	2,897,000.00	1,972,300.00
Total net worth	$8,187,000.00	$4,852,300.00

Intercompany stockholdings:

Particulars	*Owned by company* F	G
F Company stock, included in above net worth at cost to G Company—9,930 shares purchased in 1905-18 at an average cost of $110.00 per share		**$1,092,300.00**
G Company stock, included in above net worth at cost to F Company—2,880 shares purchased in 1920-21 at an average cost of $200.00 per share	**$ 576,000.00**	

Net profits:

Particulars	*Company* F	G
Net profits for five years, including intercompany dividends	**$4,234,000.00**	**$1,347,100.00**
Intercompany dividends included in above net profits	**$ 144,000.00**	**$ 695,100.00**

A owns 331 shares of F Company stock and 324 shares of G Company stock. How many shares of the preferred and common stock of H Company will he receive in exchange for his present holdings?

NORTH CAROLINA C. P. A. EXAMINATION

Commercial Law

THURSDAY, NOVEMBER 20, 1930, 9 A. M. TO 1 P. M.

CONTRACTS

Question 1:

A, a director of a corporation which had become financially involved, promises B that if B will extend credit to the corporation up to a stated amount for a certain time, he, A, "will see that B is paid." B agrees to and does extend the credit. The agreement between A and B is oral. The corporation fails to pay the account and B sues A. A contends (1) that the "statute of frauds" furnishes him a technical defense, and (2) there is no consideration. Discuss both contentions.

Question 2:

The X Coal Company sends to A, a letter, which reads in substance that the company has just received a large quantity of coal of the kind A used last year and the company will be pleased to receive A's order for his "season's requirements," which, if placed at once, will be sold to him and delivered from time to time as needed, on thirty days credit, at $8.00 a ton delivered. A, upon receiving this letter, immediately writes back that he accepts. This letter is lost in the mails. Later, upon inquiry by A, the company informs A it never got his letter, and, also, that it would not have complied with it anyway, as after sending the letter, it decided the price per ton was too low. A brings suit and the following points are to be decided:

(1) Was the letter to A an offer or only a "feeler" for trade?

(2) A contract for season's requirements is no contract at all, as A might not have any requirements.

(3) If the company's letter was an offer, A's acceptance is incomplete as it never reached the company.

Discuss these points.

Question 3:

A agrees to sell, and B to buy 50,000 shingles. Both A and B are in the lumber business. In a law suit for the price, the question is presented whether a custom of the trade in that community that a thousand shingles means a bundle of a certain size which may contain more or less, can be introduced in evidence, B contending that he might and is entitled to 50,000 shingles by actual count, and that to prove a custom to the contrary violates the parol evidence rule. Discuss, explaining what is meant by the parol evidence rule.

BANKRUPTCY

Question 1:

When is a person deemed to be insolvent under the present National Bankruptcy Act?

Question 2:

D files a voluntary petition in Bankruptcy and schedules his indebtedness to L as one of his liabilities, and notice is duly sent to L. If L desires to participate in the division of D's assets, must he file proof of his claim or is the fact that it is scheduled as a debt by D sufficient to enable L to participate in dividends?

CORPORATIONS

Question 1:

At common law can a corporation own stock in another corporation? What are the usual provisions in this regard of modern statutory law?

Question 2:

The directors of the X Corporation on September 15th, declare a dividend out of earnings, payable October 1st, to stockholders of record September 25th. On September 20th, they decide that, owing to business conditions, it will be wiser for them to omit the dividend and thus "maintain a strong cash position," and unanimously vote to rescind their former action. On October 2nd, A who was of record September 25th, brings suit for the dividend. Can he recover? In other words, when a dividend is once declared, is it rescindable?

Question 3:

In the absence of any statutory provision, or any provision in the charter or stock certificate or other express or specific provision, is preferred stock:

(a) Participating in the earnings with the common above the per cent stated, i. e., if it is 7 per cent preferred, does it participate with common in dividends above that amount?

(b) Voting?

(c) Cumulative?

(d) Preferred in the division of assets upon liquidation?

(e) Redeemable at the option of the board of directors?

Question 4:

A corporation has 1,000 shares of outstanding stock. There are three directors. The statute provides that the directors shall have power "to excercise the corporate powers." These directors decide to purchase the assets of another corporation which is in the same line of business, and which is comparatively smaller, but successful. The stockholders hold a meeting and by a two-thirds vote disapprove the purchase, pass a resolution to that effect and finally notify the directors of this action. The directors decide to ignore the action of the stockholders. A stockholder brings a suit to prevent the entering into the contract of purchase. He contends (1) that the acquisition of the business is not within the corporate powers; (2) even, if so, the directors are bound by the action of the stockholders. Is he right in either contention?

PARTNERSHIPS

Question 1:

Tom Cadillac and Peter Studebaker form a partnership for the conduct of a garage, with a department for selling parts and accessories. It is agreed between them that they will not deal in tires, as they regard that line hazardous. In Cadillac's absence, Studebaker, in violation of this agreement, buys a quantity of tires. Cadillac comes back and repudiates the purchase. The tire company asks you whether they can hold the partners on this transaction. Discuss.

Question 2:

In the above case, Studebaker is a minor, nineteen years of age. He has contributed $5,000.00 capital. He demands that Cadillac restore him this amount, although the capital assets are now only $2,500.00, and there are unpaid debts. Must Cadillac account to him for this amount?

Question 3:

In "Partnership Articles" between A and B, it is agreed that A will protect B against loss. Does this limit the rights of creditors against B?

NEGOTIABLE INSTRUMENTS

Question 1:

Joe Maker, in a transaction with Tom Payee, gives to Payee, an instrument reading as follows:

"Charlotte, N. C., Oct. 1, 1930.

"Due to Tom Payee, or order, the sum of One Thousand Dollars, two years from date, with interest at the rate of six per cent per annum. (Signed) Joe Maker."

Tom Payee indorses this note and sells it, on January 1, 1931, to Ed Holder who pays $500.00 for it and who has no knowledge that anything is wrong. Later, having learned of some irregularities in the original transaction, Holder comes to you with the following questions:

(a) Is the note negotiable or non-negotiable? Why?

(b) If, whatever your reply to (a), the court should hold the note to be negotiable, would the fact that the original transaction was usurious (it not so appearing on its face) be a defense available against Holder, who knew nothing of it when he bought the paper?

(c) Same question, if the court should hold the note to be non-negotiable?

(d) Is an indorsement on a holiday invalid?

(e) If the above note is negotiable, is the amount that Holder can recover governed and limited by what Holder paid to Payee?

Question 2:

The following note is made and delivered:

"Charlotte, N. C., Oct. 1, 1930.

"On or before one year after date, I promise to pay to Tom Payee, or his assigns, the sum of One Thousand Dollars, with interest, or if he so elects to deliver to him, or assigns, 50 shares of the common stock of the Excelsior Corporation. The maker of this note waives all exemptions to which he might be, by law, entitled." (The maker, whose name is Joe Maker, conducts an incorporated business which he calls "Dodge Street Emporium" and he uses this name in signing this note, not adding his own name or his initials.)

Tom Payee sells this note for value to Ed Holder to whom he endorses and delivers it. Holder acquires it in good faith for value and before maturity, and presents it at maturity to Maker, who declines payment on the ground that Payee broke the contract in which the note was given. Maker contends that the note is not negotiable for the following reasons:

(a) It is payable "on or before";

(b) It is not payable to order or to bearer;

(c) No rate of interest is stated;

(d) It is payable either in money or stock;

(e) It waives exemptions whereas by the law of the state such a waiver is ineffectual;

(f) It is not signed as required by the Uniform Negotiable Instruments Law.

Which, if any, of these contentions are good?

Question 3:

In what cases is "protest" necessary?

Question 4:

A bank certifies a raised check. Is it liable to an innocent taker thereof for the amount as originally stated or as it was when certified?

FEDERAL INCOME TAX

Question 1:

A's taxable income for the year 1929, as computed by his bookkeeper, is in excess of $100,000, and consists of salary, income from business, and interest. The earned income included therein exceeds $30,000. You find, however, that dividends were inadvertently omitted from the computation. The dividends received during the year 1929 were as follows:

Cash dividends from domestic corporations	$10,000.00
Property dividend from domestic corporation, at fair value of property received	1,000.00
Liquidating dividend in cash (first and final) on 100 shares of stock purchased in 1920 at $100 per share; no loss has yet been taken on the stock	2,000.00
Cash dividends from foreign corporations having no business in the United States	5,000.00

How much additional tax will A pay on the above dividends?

NORTH CAROLINA C. P. A. EXAMINATION

Auditing

FRIDAY, NOVEMBER 21, 1930, 9 A. M. TO 1 P. M.

Question 1:

In your audit of the Rex Importing Company you find three bank accounts as follows:

Cash in Austin State Bank	$5,318.27
Cash in West Town State Bank	816.38
Overdraft—Bank of America	1,837.26

How would you set up the cash in bank on your balance sheet, assuming the figures to be correct?

Would your procedure be different provided the cash in Austin State Bank was $5,000.00 less?

Question 2:

During the audit of the A Company you discover an invoice, covering merchandise purchased from the B Company, extended as $132.15, whereas the correct amount should have been $1,321.50. You adjust purchases and credit B Company $1,189.35 and subsequently give the entry to the bookkeeper.

It happens that B Company is also your client and is unaware that an error has been made. What action would you take in connection with this invoice when, at a later date, you are auditing B Company's books and discover that the A Company, in the meantime, has paid $132.15 in full settlement of the invoice? Your audit engagement with the B Company does not include an inspection of sales invoices.

Question 3:

Appearing on the books of the CD Company at December 31, 1929, are advances to salesmen in excess of commissions due, amounting to $25,652.10. Of this amount, $20,562.19 represents advances made to salesmen who have left the company. The management of the company, while admitting that the accounts are uncollectible, insists that they not be charged off at December 31, 1929, but written off monthly during 1930, due to the fact that these salesmen secured orders for future delivery. What attitude would you take in this matter?

Question 4:

An argument has arisen between an accountant and a banker regarding the position of disclosures and qualifications pertaining to a certified balance sheet. The accountant has prepared a balance sheet which is very long and on which numerous items have been qualified. At the bottom of the balance sheet a brief certificate appears. The banker believes that the balance sheet is too bulky; he admits the necessity for the qualifications but prefers to see them in the certificate even though the latter attains a length of several pages. The result, he says, is a more easily read balance sheet.

What is your opinion?

Question 5:

A manufacturer of ice cream purchased, on the deferred payment plan, refrigerator units at a cost of $15,100.00. All these units were resold to customers at cost. Collections from the customers in payment of the units had been $3,126.18, while payments by the manufacturer to the distributor of the units totaled $6,180.31.

You are auditing the books of the manufacturer who contends that he has no liability to the distributor because he purchased the refrigerator units for his customers and that an asset should appear on his balance sheet as follows:

Advances to customers—	
Payments made for customers' account	$6,180.31
Less—Cash received from customers	3,126.18
Balance	$3,054.13

Do you believe that your client is correct in his contentions?

Question 6:

The Rosy Apple Company, engaged in the fruit commission business, has an arrangement with the bank whereby drafts drawn on customers for carloads of fruit shipped to them are immediately credited to the company's bank account. Any drafts upon which payment is refused are charged back to the company when notice is received from the correspondent bank. In making an audit of the company at December 31, 1929, what disposition would you make of any drafts unpaid at that date?

Question 7:

The fiscal year of an investment trust ends September 30, 1930. Because of depressed financial conditions on that date, the market values of all its investments are below cost. The management, while willing that you should state on the balance sheet that securities are valued at cost, asks you to withhold all comment regarding market prices. What attitude would you take as auditor?

Question 8:

The demand note evidencing a bank loan of the company you are auditing has been endorsed by the president of the company. It is explained that a collateral loan is thus avoided.

Should the balance sheet of the company reflect the endorsement?

Question 9:

The following situation was disclosed in the audit of The National Manufacturing Company for the year ending June 30, 1930:

The sum of $50,000.00 was borrowed from the president of the company on January 8, 1930, and was repaid on January 28, 1930. At the end of June, however, this check was still outstanding and upon inquiry the auditor learned that the president was holding the check until the company was in a better financial position. The books reveal that there is an overdraft of $36,182.12 in the bank account.

How should this transaction be handled on the financial statements prepared by the auditor?

Would your procedure be different if the bank account per books showed a balance of $8,629.31 instead of an overdraft?

NORTH CAROLINA C. P. A. EXAMINATION

Practical Accounting

FRIDAY, NOVEMBER 21, 1930, 2 TO 6 P. M.

Problem 1:

In auditing the books of a manufacturing company for the year ending December 31, 1929, you find the following situation in connection with the machinery account:

No fixed rate of depreciation has been used, the company arbitrarily writing off a certain amount each year and crediting the asset. The proper annual rate for this type of machinery may be assumed to be 8%.

Machine C was considered to have a life of 10 years after it was completely overhauled on August 1, 1929.

An appraisal was made by the A Appraisal Company as of December 31, 1929, with the following result:

Machine	Cost of reproduction	Reserve for depreciation	Net sound value
A	$12,000.00	$ 7,680.00	$ 4,320.00
C	18,000.00	7,860.84	10,139.16
D	7,000.00	4,480.00	2,520.00
E	8,000.00	1,151.33	6,848.67
F	11,500.00	1,150.00	10,350.00
G	15,000.00	500.00	14,500.00
Totals	$71,500.00	$22,822.17	$48,677.83

The following entry appears on the records:

Machinery account	$14,500.00	
Surplus	8,322.17	
Reserve for depreciation		$22,822.17

To set up results of appraisal made December 31, 1929, by the A. Appraisal Company.

Assuming that the Board of Directors have voted to adjust the books to the appraisal figures, do you believe that the entry is correct? If not, make the necessary adjusting entries, with complete explanation, to put the books on the proper basis.

Analysis of the machinery account follows:

MACHINERY ACCOUNT

Debits			
1—1—1922	Machine A	$10,000.00	
1—1—1923	Machine B	12,500.00	
1—1—1924	Machine C	16,000.00	
1—1—1925	Machine D	8,000.00	
5—1—1927	New motor for Machine A, replacing motor which cost $1,200.00, included in original cost of machine	1,800.00	
11—1—1927	Rewinding of burned-out coils of motor on Machine B	350.00	
3—1—1928	Machine E	7,850.00	
10—1—1928	Machine F	11,500.00	
8—1—1929	Machine G	15,000.00	
8—1—1929	Complete overhauling of Machine C	3,500.00	
8—1—1929	Cost of changing positions of Machines C and D so as to place Machine G in the most efficient position	2,000.00	
12—31—1929	Appraisal	14,500.00	$103,000.00

Credits			
12—31—1922	Depreciation	$ 4,000.00	
12—31—1923	Depreciation	2,000.00	
12—31—1924	Depreciation	10,000.00	
12—31—1925	Depreciation	8,000.00	
12—31—1926	Depreciation	1,000.00	
12—31—1927	Depreciation	2,000.00	
12—31—1928	Depreciation	2,000.00	
8— 1—1929	Allowance on Machine B traded in on purchase of G	2,500.00	31,500.00
	Balance in asset December 31, 1929, per appraisal		$71,500.00

Problem 2:

John M. Good, a merchant, has called you in to review his individual Federal income tax return for the calendar year 1929, which was prepared by his bookkeeper. Aside from his business proprietorship, no books were kept.

Mr. Good is a citizen of the United States, maintaining his home in Chicago, Illinois. He is the father of two children in school, neither of whom contribute to their own support, one seventeen and the other twenty years of age.

Mr. Good's wife, Mary B. Good, died August 5, 1929. The administrator of her estate filed an individual Federal income tax return for her covering the period up to and including the date of death. On the individual return he deducted $3,500.00 for personal exemption.

The bookkeeper has computed Mr. Good's tax as follows:

Particulars	*Amount*	
INCOME:		
Salary	$ 3,600.00	
Income from business	32,540.76	
Interest on deposits, bonds, etc.	12,172.48	
Rents and royalties	2,210.65	
Profit from sale of real estate, stocks, bonds, etc.	90,671.30	
Dividends on stock	5,720.52	
Income from fire insurance	1,778.40	
Total income		$148,694.11
DEDUCTIONS:		
Interest paid	$2,648.73	
Taxes paid	3,017.21	
Bad debts	2,000.00	
Contributions	600.00	
Total deductions		8,265.94
Net income		$140,428.17

COMPUTATION OF TAX

Net income		$140,428.17
Less—		
Dividends	$5,720.52	
Credit for dependents	800.00	
Personal exemption	3,500.00	10,020.52
Balance		$130,407.65

Normal tax—1½%	on $4,000.00	$ 60.00
3%	on next $4,000.00	120.00
5%	on balance of $122,407.65	6,120.38
Surtax of 20% on $140,428.17		28,085.63
		$ 34 386.01
Less—Credit of 25% on earned income		422.00
Net tax		$ 33,964.01

You determine the following facts pertinent to the situation:

The salary of $3,600.00 was received from the D Corporation of which Mr. Good is an officer and director.

Income from a private business of Mr. Good's was computed as follows:

Particulars	*Amount*	
Total receipts		$781,426.38
Cost of merchandise sold (net)	$525,469.09	
Salaries	100,048.60	
Interest	6,211.14	
Taxes	895.32	
Bad debts	9,410.16	
Depreciation	14,786.92	
Rent, repairs and other expenses	92,064.39	748,885.62
Net profit		$ 32,540.76

Receipts included $150.00 from the sale of certain old fixtures which had originally cost $1,355.00, and, including the writeoff for 1929, had been depreciated by $1,005.00. The fixtures had not been removed from the asset account on the books of the business.

Other business expense included $728.48, the cost of repairs and upkeep of Mr. Good's automobile which was used for business purposes about 75% of the time.

Interest income included:

Particulars	*Amount*
On bank deposits	$ 769.48
From industrial bonds	5,388.00
From utility bonds	4,365.00
From Cook County Highway bonds	1,650.00
	$12,172.48

All utility bonds owned by Mr. Good were tax-free-covenant issues on which a 2% tax had been paid at the source.

Rents were analyzed as follows:

Particulars	Amount received	Cost of asset	Depreciation	Repairs	Other expense	Net profit
Building A	$16,245.00	$192,645.00	$3,852.90	$3,621.16	$6,480.03	$2,290.91
Building B	6,000.00	78,240.00	1,564.80	1,195.20	3,320.26	*80.26
						$2,210.65

* Red

The loss from Building B was attributed to the fact that Mr. Good occupied one of the six apartments in this building and that no income was realized from that apartment.

Profit from sale of real estate, stock, bonds, etc., was made up of the following items:

	Date acquired	Amount received	Depreciation allowable	Cost	Subsequent improvements	Net profit
Factory building	1928	$73,425.00	$12,865.80	$77,349.50	$7,480.00	$1,461.30
Stock rights (Master Corp.)	1929	210.00				210.00
Barrington Mach. stock.	1925	110,500.00		21,500.00		89,000.00
						90,671.30

The 20 stock rights (one right had been received for each 5 shares held) were sold at $10.50 each and had been acquired as the result of the ownership of 100 shares of Master Corporation stock purchased in 1922 by Mr. Good at $93.00 per share. The market price of the stock at the time the rights were issued was $138.00 per share and the market value of the rights was $7.50 each. The proper proportion of cost should be allocated to the rights.

Dividends were received from:

200	shares M and M Bank stock	$3,000.00
50	shares Belding Foundry stock....................	175.00
82 5-6	shares Jordan Building Co. stock	538.52
60	shares Hemple & Co. stock....................	2,007.00
		5,720.52

Hemple & Company had discontinued business in 1928 and the dividend received in 1929 was the first liquidating dividend. The stock had been purchased at par ($100.00) in 1920.

Income from fire insurance was received as compensation for damage done to a garage which was entirely destroyed by fire. The garage was built by Mr. Good at a cost of $1,890.00 on which depreciation of $629.50 had been taken. After the fire the structure was rebuilt at a cost of $2,118.00.

Interest expense of $2,648.73 covered personal borrowings and included $378.15 of accrued interest. Taxes paid were as follows:

Personal property	$ 216.85
Real estate, including $1,047.60 of special new paving assessment..............	2,800.36
	$3,017.21

Real estate tax bills of $4,932.60, including $1,998.57 of special paving assessments were due but unpaid.

The $2,000.00 bad debt consisted of money loaned to Mr. Good's brother in 1928. There was no note to support the loan. The brother's death in 1929 precluded the possibility of collecting; Mr. Good did not desire to press the claim because the net estate going to the widow was only $5,000.00. Contributions were made up as follows:

Church	$350.00
Y. M. C. A. building fund....................	50.00
Salvation Army Christmas chest....................	50.00
Democratic party campaign fund....................	150.00
Total	$600.00

Recompute Mr. Good's income tax liability, prepare the necessary supporting schedules, and explain any differences between your figures and those of the bookkeeper.

The applicable surtax rates in force during 1929 were:

Income	Rate applicable to last bracket of income	Total surtax
$14,000.00	1	$40.00
16,000.00	2	80.00
48,000.00	12	2,720.00
52,000.00	13	3,240.00
56,000.00	14	3,800.00
60,000.00	15	4,400.00
64,000.00	16	5,040.00
70,000.00	17	6,060.00
80,000.00	18	7,860.00
100,000.00	19	11,600.00
100,000.00 +	20	—

Probelm 3:

The Coldwater Salt Company is contemplating a change in its capital structure with a view to reducing the charge to surplus for dividends on its 7 per cent preferred stock. The capitalization of the company at July 1, 1930, was as follows:

	Authorized	*Issued*
7% cumulative preferred stock, par value $100.00 per share..........	$500,000.00	$300,000.00
6% preferred stock, par value $50.00 per share....................	250,000.00	100,000.00
Common stock, no-par value	25,000 sh	10,000 sh

Two alternatives have been suggested for eliminating the 7 per cent preferred stock:

(1) Issuance of $300,000.00 20-year 5 per cent first mortgage bonds at 92. Under the present market conditions a 2 per cent tax-free covenant would be necessary to effect their sale.

(2) Offering of rights to common stockholders to purchase one and one-half shares of common stock for each share now held at its stated value, namely $20.00 per share.

The 6 per cent preferred stock and the common stock were issued at par and at the above stated value, respectively, at the time of incorporation in 1923. The 7 per cent preferred stock was issued in 1925 at 95. Since that time the directors have authorized the writing off of amounts of the discount as follows:

Date	*Amount*
December 31, 1926	$5,000.00
June 30, 1928	2,500.00
December 31, 1929	1,500.00
Total..	$9,000.00

The common stock is on a $2.00 annual dividend basis, and, should any new common stock be issued, it is expected the rate will remain unchanged.

The annual net profits of the company before deducting Federal income taxes have averaged $90,000.00, and, considering the inelasticity of the business, it is estimated that in the future there will be no radical variations. You may assume that the Federal income tax will remain at 11 per cent.

On October 1, 1930, the directors of the company ask you to prepare a statement showing the effect of these projected changes upon the earnings applicable to common stock. If they are satisfied that a saving can be effected, they will call the necessary directors' and stockholders' meetings and secure the proper authorization from the Secretary of State so that the new capitalization may take effect as of January 1, 1931.

Prepare such a statement.

NORTH CAROLINA C. P. A. EXAMINATION

Practical Accounting

SATURDAY, NOVEMBER 22, 1930, 9 A. M. TO 1 P. M.

Problem 1:

From the detail appearing below, taken from the records of the Conway Conversion Company (a) determine the correct net profit for each of the five years shown, and prepare (b) a statement of surplus as revised for the five-year period ending December 31, 1929, and (c) an adjusting journal entry as at December 31, 1929, to bring the books into agreement with your figures.

CONWAY CONVERSION COMPANY
ANALYSIS OF SURPLUS FOR FIVE YEARS
January 1, 1925—December 31, 1929

Date		Debit	Credit
Jan. 1, 1925	Balance		$191,265.17
April 4, 1925	Dolan suit settled (damages allowed by court March 15, 1925, to injured employee not covered by insurance—suit started in 1924. On December 31, 1924, attorneys of company submitted an opinion that no liability existed)	$5,450.00	
Aug. 2, 1925	Additional Federal income tax assessment for calendar years 1920-1921	1,148.60	
Dec. 31, 1925	Profit and loss from operations		137,648.70
Jan. 2, 1926	Dividends	150,000.00	
Feb. 1, 1926	J. M. Walters—Balance of commissions; 1925 sales liability not determined at close of year	1,700.49	
June 30, 1926	Adjustment of accounts receivable control (bringing control into agreement with detail		89.10
Aug. 18, 1926	Appreciation of plant values (see appraisal of Messrs. King, Cole and Wood)		110,469.26
Nov. 11, 1926	Adjustment of accrued tax account (anticipated tax on real estate over-estimated, December 31, 1925)		2,354.00
Dec. 28, 1926	Christmas bonus for employees	17,500.00	
Dec. 31, 1926	Profit and loss from operations		235.681.14
Jan. 3, 1927	Dividend	150,000.00	
April 30, 1927	Cost of repairing roof damaged by windstorm in April, 1927	4,819.60	
July 7, 1927	Extra dividend	100,000.00	
Oct. 31, 1927	Cash received for boring machine purchased January 1, 1920, for $3,950.00, and depreciated up to date of disposal by $3,520.00 (never written off books)		1,000.00
Dec. 31, 1927	Profit and loss from operations		180,472.88
Jan. 10, 1928	Dividend	150,000.00	
May 30, 1928	Additional Federal income tax assessments and credits—		
	1922	742.11	
	1924		178.52
	1925	1,004.06	
June 30, 1928	Extra dividend	100,000.00	
Nov. 30, 1928	Appreciation of value of various securities owned by company to market value		72,580.00
Dec. 31, 1928	Profit and loss from operations		112,043.17
Jan. 16, 1929	Dividend	150,000.00	
April 30, 1929	Cost of replacing faulty material manufactured and sold in—		
	1927	6,510.97	
	1928	12,518.20	

April 30, 1929	Interest accrued not on books at December 31, 1928	1,725.34	
June 30, 1929	Extra dividend	50,000.00	
Oct. 31, 1929	Loss on sale of securities (all holdings disposed of)	89,562.75	
Nov. 15, 1929	Financing charge on two-year note dated November 15, 1929	10,000.00	
Nov. 30, 1929	Additional assessment Federal income taxes—		
	1926	2,610.19	
	1927	514.27	
Dec. 31, 1929	Depreciation of inventory to market prices	54,243.06	
Dec. 31, 1929	Bell & Company bankrupt—Account uncollectible	12,900.00	
Dec. 31, 1929	Profit and loss from operations		55,218.44
	Balance	26,050.74	
		1,099,000.38	1,099,000.38

Investigation indicates that depreciation of plant and equipment had been provided on a percentage of sales. The following schedule reflects the depreciation charged and the proper computation according to standard rates:

Year	Charged off per books	Correct charges
Prior to 1925	$198,313.20	$183,617.38
1925	37,724.48	35,520.16
1926	68,419.26	40,113.09
1927	49,200.41	42,301.47
1928	28,653.97	43,662.51
1929	20,135.60	44,728.96
Totals	402,446.92	389,943.57

An examination of vouchers and physical inventories disclosed the fact that certain items had been taken up in inventories that had not been entered in the voucher register until the following period; also that a number of purchases had not been given expression to on the inventory, although the materials had been vouchered and were on hand at the close of the period. Below is an analysis of this condition:

Date December 31—	Material in inventory but not in voucher register	Materials vouchered but omitted from inventory
1924	$ 756.28	
1925	3,620.40	
1926		$1,182.15
1927	9,417.38	2,046.50
1928	14,691.07	
1929		3,912.63
Totals	28,485.13	7,141.28

Interest accrued and interest prepaid had not been expressed on the books at the close of the various years; the proper computation being found to be:

Date December 31—	Interest accrued	Interest prepaid
1924		$ 428.15
1925	$ 591.10	1,617.30
1926	948.78	1,145.26
1927	1,993.93	633.27
1928	1,725.34	
1929	4,860.55	
Totals	10,119.70	3,823.98

Bad debts and bad debt recoveries had not been handled on a reserve basis. It was deemed advisable to place the company on a reserve basis; following are the correct charges and the actual amounts charged and credited to profit and loss:

Year ending December 31	Bad debts charged off to profit and loss	Credits to profit and loss for bad debt recoveries	Correct charges to expense on reserve basis
Balance—1924			$8,182.50
1925	$1,421.16	$169.20	6,926.58
1926	10,660.42	116.79	7,837.85
1927	2,952.68	259.43	7,615.23
1928	5,653.22	40.06	5,764.02
1929	3,856.77	178.52	8,971.45

Insurance on officers' lives on which the company was the beneficiary carried cash surrender values which had not been capitalized. The total cash surrender value on December 31 of each year was as follows:

Date December 31—	Total cash surrender value
1924	$4,550.90
1925	6,142.07
1926	7,783.27
1927	9,484.47
1928	11,229.47
1929	13,039.62

Problem 2:

From the information that follows you are required to furnish the following information and statements:

(1) Adjusting journal entries to correct the books and to record the sale;

(2) Statement of profit and loss for the six-months' period, including therein the proper liability for Federal income tax;

(3) Balance sheet as at October 31, 1930.

Maple Hotels, Inc., was incorporated under the laws of the State of Ohio on April 30, 1929, to take over the assets and liabilities of the partnership of Smith and Brown. The partnership had financed and built the Maple Hotel and completed it at the date of incorporation. The land and building were conveyed to the corporation at a valuation of $471,551.50; the land at $70,000.00, which was cost to the partnership, and the building at an appraised valuation of $401,551.50, which was $200,000.00 in excess of cost. All other assets and liabilities were conveyed and maintained at book values. In exchange for the net assets of the partnership as above mentioned, Smith and Brown received all the stock, except one qualifying share of the Maple Hotels, Inc.

On May 1, 1929, Maple Hotels, Inc., leased the building, unequipped, to private parties for 20 years at an agreed rental, receiving as a bonus thereon $20,000.00 in cash.

As at October 31, 1930, the Maple Hotels, Inc., sold the land and building, subject to the lease, receiving from the buyer a building site on H Street valued at $225,-000.00, and additional cash to balance the equities of the parties. The closing statement from the broker and the trial balance (before recording the sale) taken from the books of account of the corporation follow:

BROKER'S CLOSING STATEMENT, OCTOBER 31, 1930

Debit—Seller		*Credit—Buyer*	
Land	$225,000.00	7% first mortgage bonds (an instalment of $1,000, was paid November 1, by Maple Hotels, Inc.)	$179,000.00
Unpaid special assessments for intercepting sewer, H street property	400.00	Unpaid special street assessments, Maple Hotel	149.36
Estimated real estate taxes, year 1930, H street property	1,000.00	Accrued interest on bonds	2,846.50
Unexpired insurance, Maple Hotel	3,875.24	Estimated real estate taxes, year 1930, Maple Hotel	2,750.00
		Cash, to balance	45,529.38
	$230,275.24		$230,275.24

Maple Hotels, Inc., received $35,529.38 in cash, the difference representing a commission to the broker of $9,000.00 on the sale and attorney fees of $1,000.00. The latter includes legal fees of $250.00 relating to the organization of the company, not yet appearing on the books.

TRIAL BALANCE, OCTOBER 31, 1930

Lake Trust and Savings Bank	$ 317.18	
Loans to stockholders	5,499.08	
Unexpired insurance premiums, Maple Hotel	3,928.90	
Land, State Street, at cost	45,000.00	
Preliminary plans, State Street Building (contemplated)	2,800.00	
Land, Maple Hotel	71,884.97	
Building, Maple Hotel (estimated life, 50 years)	401,551.50	
Reserve for depreciation on building, Maple Hotel		$ 6,046.54
Bank loans and notes payable		22,800.00
Accounts payable		3,374.08
Accrued real estate taxes, Maple Hotel		2,375.24
Accrued interest on bonds, Maple Hotel		2,871.00
Accrued interest on notes		52.58
7% first mortgage bonds on Maple Hotel ($1,000.00 due the fifth of each month during 1930)		180,000.00
No-par value common stock, 10,000 shares		296,396.02
Operating loss, year ending April 30, 1930	3,660.40	
Deferred bonus income on Maple Hotel lease		18,500.00
Organization expenses	500.00	
Rents received, Maple Hotel lease		15,000.00
Income realized on Maple Hotel lease bonus		500.00
Salaries and wages	716.21	
Insurance expense	691.20	
Building repairs, Maple Hotel	905.53	
Real estate taxes ($250.00 per month) expense	1,500.00	
Depreciation on building	2,015.51	
Interest on bonds and notes	6,235.40	
Miscellaneous office expenses	709.58	
	$547,915.46	$547,915.46