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American Institute of Accountants. Board of Examiners

American Institute of Accountants Examinations

[Following is the text of the examinations in auditing, law and accounting presented by the board of examiners of the American Institute of Accountants November 13 and 14, 1930.]

Examination in Auditing

November 13, 1930, 9 a. m. to 12:30 p. m.

No. 1 (10 points):

Under which, if any, of the following conditions would you permit interest to be considered a part of manufacturing cost and of inventory valuation? State the general governing principle. Give reasons.

(a) A manufacturing company in leasing its premises in lieu of a fixed rental pays the lessor a stipulated rate of interest upon his investment in the premises plus a royalty upon the quantity of products manufactured.

(b) A timber company, having held a tract of timber for a long period, has capitalized the interest upon the mortgage on the timber; and now, upon manufacturing the timber into lumber, proposes to write off depletion based on book values.

(c) A sugar plantation and factory, newly organized, has set up interest on money borrowed to raise its first sugar-cane crop as part of the cost of the crop during the two years required to raise it.

(d) A cocoanut-oil manufacturer buys copra in the Philippines, accepting in settlement an interest-bearing draft which is forwarded by the sellers to their bankers in San Francisco with bill of lading attached. The same copra could have been purchased f.o.b. San Francisco at a higher price.

No. 2 (10 points):

State how you would proceed in making a detailed audit of a bank.

No. 3 (10 points):

One of the duties of an auditor is to ascertain whether or not any liabilities exist which are not shown on the books. What procedure would you follow?

No. 4 (10 points):

In auditing the accounts of a corporation for the first year of its existence what records and documents should be examined before starting on the regular books of account? State reason for each step.

No. 5 (10 points):

The following certificate was appended to the consolidated balance-sheet of the Blank Corporation and its subsidiaries:

We have examined the books and accounts of the Blank Corporation and its domestic and South American subsidiaries and affiliated companies for the year ended December 31, 1929, and have had submitted to us the audited statements of the remaining foreign subsidiary companies. The assets and liabilities of subsidiary companies other than the South American companies are embodied in the above balance-sheet. South American and affiliated companies are treated as investments. In accordance with the decision of the directors, no charge for depreciation of plants was made during the year. We certify that upon the foregoing basis the balance-sheet is in our opinion correctly prepared so as fairly to set forth the financial position of the companies at December 31, 1929.

What qualifications are there in the above certificate?

No. 6 (10 points):

The Y Corporation on December 31, 1929, shows the following balances in its accounts with banks:

1st Nat.	Debit bal.	$20,000
2nd "	Overdraft	5,000
5th "	Debit bal.	10,000
	Total agreeing with cash account	$25,000

State how you would show these balances on your balance-sheet and explain why.

In what circumstances would you modify your decision?

No. 7 (10 points):

The X Corporation was organized in 1914 with a capital stock of $10,000, paid in cash, and all owned by John Doe, unmarried and without dependents. By 1925 it had accumulated a surplus of $50,000. The capital stock was then increased to $50,000, and a stock dividend of $40,000 was declared and paid to John Doe. During the next four years the average profit from the business, after deducting a salary of $10,000 a year to John Doe as president and general manager, was $2,500 a year, so that on December 31, 1929, the net assets of the corporation were $70,000, represented by $50,000 capital stock and $20,000 surplus, all of both being invested in plant and equipment.

In addition to the federal income tax, the corporation pays a state property tax of ½% on the book value of its capital stock; and John Doe, of course, pays a federal normal tax and surtax on his salary plus other income.

In 1930, exasperated by the increasing taxes and the annual state and federal reports he must make on behalf of the corporation, John Doe consults his lawyer who advises him to liquidate the corporation by turning in his stock in exchange for the net assets, to surrender its charter, and thereafter to conduct business individually.

You are engaged to supervise the accounting details of the proposed reorganization, and your opinion of the lawyer's suggestion is asked.

What would you advise, and why?

No. 8 (10 points):

You are auditing the accounts of a restaurant and find that the cost of food supplies is too high in proportion to the receipts from sales.

The restaurant is on the street level of an office building in a busy district of the city. There are four entrances to the restaurant, one on each of three different streets and one from the office building. There is a receiving cashier at each entrance, and cash registers are used. All meals are served at tables and bills are given to customers who make all payments to the cashiers. The kitchen is separated from the dining-room, and two doors are used for service both ways. As the restaurant is open 16 hours daily there are two shifts of employees.

The kitchen manager, who buys all food supplies, contends that the kitchen has issued more meals than have been accounted for in the receipts.

You are asked to suggest a method by which all food taken from the kitchen can be accounted for more exactly. The method suggested must not increase the expense, it must not affect the speed of service in rush hours, and the number of entrances must not be reduced.

What would you suggest?

No. 9 (10 points):

You are engaged to draw up a partnership agreement for a firm about to be organized. State at least ten important points to be covered in such an agreement.

No. 10 (10 points):

In making a balance-sheet audit of the A B Corporation you have received a certificate, signed by the president and general manager, of inventory amounting to $60,000, which you have tested to your satisfaction as to prices and clerical accuracy. Later before the close of the audit you discover that the corporation has filed an income-tax return showing an inventory of $50,000.

What will you do?

Examination in Accounting Theory and Practice

PART I

NOVEMBER 13, 1930, 1 P. M. TO 6 P. M.

The candidate must answer the first three questions and one other question.

No. 1 (35 points):

From the information following, prepare:

(a) Journal entries, recording the purchase of the investments at April 1, June 30 and September 1, 1929.

(b) Statement showing amount of goodwill and capital surplus arising from consolidation, as at December 31, 1929.

In making an audit of the books of account and records of the Smith Theatre Company and its subsidiaries—the Brown Pictures, Incorporated, and the Green Amusement Company—for the year ended December 31, 1929, you find the following conditions:

The Brown Pictures, Incorporated (hereafter alluded to as "the corporation"), was organized January 1, 1929. The incorporators, owners of theatres in favorable locations, leased their theatres, with equipments, to the corporation for a period of twenty years commencing January 1, 1929, and received, in consideration therefor, all the capital stock of the corporation in addition to an annual fixed rental payable by the lessee in equal monthly instalments in advance on the first day of each month.

The capital stock of the Brown Pictures, Incorporated, consists of 10,000 shares of no par value and was issued, according to the articles of incorporation, for leaseholds appertaining to the leased theatres, appraised by the incorporators at date of organization at $120,000. With reference to the issue of the stock, you find the following journal entry on the books of the corporation:

Leaseholds........................	$120,000	
To capital stock.................		$120,000

You also find that during the year 1929, the corporation has amortized the leaseholds by charges to profit-and-loss account on the basis of the lives of the leases.

On April 1, 1929, the Smith Theatre Company purchased from individual stockholders of the Brown Pictures, Incorporated, 5,000 shares of the capital stock of that corporation for $70,000 in cash, and on September 1, 1929, acquired from the remaining stockholders the balance of the stock, which was paid for in the following manner:

(a) 100 shares of the Smith Theatre Company's no-par-value common stock held in the treasury, purchased at $35 a share, the market value being $45.

(b) A sum in cash equal to the increase in the rental under an amendment of the lease of the Star Theatre, one of those originally leased to the Brown Pictures, Incorporated, which had been rented by the Brown Pictures, Incorporated, at date of organization from the stockholders now desirous of selling their stock. The original Star Theatre lease agreement provided for a rental of $60,000 per annum and stipulated that the corporation deposit with the lessors the sum of $60,000 bearing interest at 6 per cent. per annum, which was to be applied as rental for the last year of the term. The deposit was made by the corporation on January 1, 1929. The amended lease agreement contained the following provisions:

Term—October 1, 1929, to December 1, 1948
Rental—$72,000 per annum from Oct. 1, 1929, to Sept. 30, 1939
$70,000 per annum from Oct. 1, 1939, to Dec. 1, 1947
(payable as in the case of the first lease)
$60,000 for the balance of the term, covered by the lease deposit originally made by the lessor.

The original lease was canceled and settlement for the lease deposit was made in cash.

(c) Cancellation of the interest accrued on the lease deposit from January 1, 1929, to September 1, 1929, the amount thereof to be credited to the Brown Pictures, Incorporated.

The Green Amusement Company was organized January 1, 1929, with an authorized capital stock of 1,000 shares of no par value issued for cash, in amount $35,000. This company was indebted to the Smith Theatre Company on a note of the face value of $15,000. Owing to the unsatisfactory financial condition of the Green Amusement Company, the Smith Theatre Company accepted the note only after endorsement thereof by 95 per cent. of the stockholders of the Green Amusement Company.

With consent of the Smith Theatre Company, the endorsers of the note, anxious to free themselves of their contingent liability, which was likely to become actual, entered into an agreement on June 30, 1929, with the Brown Pictures, Incorporated, whereby they sold to that corporation all their capital stock of the Green Amusement Company upon condition that the Smith Theatre Company cancel the note and that the Brown Pictures, Incorporated, assume the liability therefor on open account.

The books of the respective companies were closed quarterly. An analysis of the surplus accounts at December 31, 1929, was as follows:

	Smith Theatre Co.	Brown Pictures, Inc.	Green Amusement Co.
Balance—January 1, 1929 (as certified by you)	$ 840,000		
Profits or losses (*):			
3 months ended Mar. 31, 1929	150,000	$120,000	$ 5,000*
3 " " June 30, "	140,000	130,000	9,000*
3 " " Sept. 30, "	175,000	135,000	12,000*
3 " " Dec. 31, "	178,000	140,000	15,000*
Balances—December 31, 1929	$1,483,000	$525,000	$41,000*

The capital stock of the Smith Theatre Company consists of 10,000 shares of no-par-value common stock, issued at $15 a share.

Wherever it becomes necessary, in your calculations, to assume an interest rate, use 6 per cent. per annum.

The profits or losses for the three months ended September 30, 1929, may be assumed to have occurred in equal amounts by months.

Given:

The present worth of an annuity payable $1.00 monthly for ten years, the first payment to be made in one month, is $90.075. The present worth of an annuity payable $1.00 monthly for eight years and two months, but with the first payment of the annuity beginning in ten years, or directly after the former annuity ceases, is $42.500083.

No. 2 (30 points):

Following, is the trial balance of the recently organized Glenview Golf Club as at December 31, 1929:

	Dr.	Cr.
Cash in bank	$ 7,225	
Accounts receivable, members	11,160	
Buildings	54,500	
Equipment	8,500	
Golf-course construction	130,000	
Labor	26,285	
Golf-course supplies and expense	12,446	
General expense	4,213	
Interest paid	5,617	
Rent	6,000	
Commissions—soliciting membership	1,100	
Notes payable—bank		$ 10,000
Accounts payable		2,341
Entrance fees		146,250
Dues		22,950
"Green" fees		5,015
Taxes on dues and entrance fees		490
Entrance fees underwritten		80,000
	$267,046	$267,046

A proprietary membership in the club costs $1,000, plus $100 tax.

An analysis of entrance-fees account shows that it includes $110,000 paid in, fully paying 110 memberships, and $36,250 collected from 60 members. The balance due from these 60 members, plus the tax thereon, is secured by notes for their original unpaid balance. These notes are on hand but not entered.

In September, 1929, a special committee, appointed for the purpose, handed in a statement with a list of 80 members, each of whom promised to obtain a new member and to advance the entrance fee of such member at once, subject to repayment when the new member paid in his fee; accordingly, the following entry was then made:

Accounts receivable, members	$80,000	
To entrance fees underwritten		$80,000

Of the above $80,000, $70,000 had been collected from the underwriters at December 31, 1929. Nothing had been repaid to the underwriters on account of new members, although 10 such new members had been elected in December and had paid in $8,800 in cash and signed notes for $2,200 for entrance fees and taxes.

Dues are $200 a year, plus 10 per cent. tax, payable quarterly in advance, and have been chargeable and entered on April 1, July 1 and October 1, 1929.

Included in "accounts receivable, members," are accounts totaling $330 for dues and taxes against 2 members who have been delinquent for nine months, and accounts aggregating $770 for dues and taxes of 8 other members. Collections can be enforced only by deduction from the proceeds of sale of such memberships after the complement of 300 members is attained.

The building account includes:

Caddy and locker house	$10,000
Architect's plans for a club house, discarded as proposal appeared too expensive	3,000
Architect's fees for new house	1,500
Payments under a cost-plus contract for the club house (under construction December 31, 1929) with a guaranteed maximum cost of $50,000	40,000
	$54,500

The golf course was finished and opened on June 30, 1929. At that date, the club being obliged to maintain the course since the original construction contract was completed, the operating accounts stood as follows:

Debits—	
Labor	$10,116
Golf-course supplies and expense	4,539
General expense	916
Interest paid	2,890
Rent	6,000
Credits—	
Dues	5,950

The club leases its real estate, for which it pays an annual rental of $6,000, payable January 1st in advance.

The estimated life of the equipment is five years from June 30, 1929.

Of the liability on the books for taxes on dues, $390 is now payable to the collector of internal revenue, representing collections in December.

Prepare the journal entries which should be made on the books as of December 31, 1929, and January 1, 1930, disregarding closing entries, as the fiscal year ends June 30th.

Submit, also, statement of assets and liabilities as of the opening of business on January 1, 1930.

No. 3 (20 points):

You are called upon to audit the books of account and records of the S. P. mills for the year 1929 and are given a copy of the trial balance, taken from the books as at December 31, 1929, before closing, which is as follows:

	Dr.	Cr.
Cash in bank and on hand	$ 12,205	
Accounts receivable	118,496	
Yarn	28,607	
Goods in process	104,293	
Supplies	9,467	
Fuel	275	
Finished goods	99,097	
Insurance prepaid	904	
Interest prepaid	1,205	
Plant and equipment	276,433	
Accounts payable		$ 55,535
Notes payable		110,000
Labor accrued		1,521
Reserve for depreciation		29,875
Reserve for contingencies		2,000
Capital stock		206,000
Surplus		104,456
Labor—weaving	55,234	
" —finishing	20,429	
Supplies used	4,210	
Repairs to machinery	3,407	
Power and light	10,249	

Fuel	$ 5,200	
Insurance	1,620	
Taxes	4,194	
Depreciation	9,998	
Factory overhead applied		$ 161,908
Sales		641,455
Discounts and allowances	2,788	
Cost of goods sold	482,018	
Commissions—selling	24,298	
Salaries—executive	8,783	
" —office	6,104	
Office and general expenses	1,684	
Interest	7,132	
Dividend on preferred stock	14,420	
	$1,312,750	$1,312,750

In the course of the audit you discover (1) that machinery which cost $4,280 was sold for $1,720, cash, and this amount was credited to plant-and-equipment account (depreciation taken thereon amounted to $1,284); (2) that among the accounts receivable an account of $12,925 for goods billed at regular selling prices actually represented merchandise on consignment (the inventory value of this merchandise was determined to be $8,404); (3) that prepaid insurance was in excess to the extent of $121; (4) that depreciation charged was overstated by $624, and (5) that accrued labor (finishing department) was understated by $506.

Before making the corrections necessary from the above findings, you decide to verify the inventories and make an analysis of the merchandise accounts. From this analysis, you establish the following:

Goods in process (manufacturing)

Inventory—January 1, 1929	$103,802	
Yarn used	317,805	
Overhead applied	161,908	
Finished goods, transferred (see below)		$477,164
Waste sold		2,058
Inventory—December 31, 1929		104,293
	$583,515	$583,515

Finished goods

Inventory—January 1, 1929	$103,951	
Merchandise transferred (see above)	477,164	
Cost of goods sold		$482,018
Inventory—December 31, 1929		99,097
	$581,115	$581,115

From the data given and facts disclosed prepare and submit your working-sheet, setting forth thereon all requisite adjustments, and present profit-and-loss statement.

No. 4 (15 points):

Several companies, manufacturing the same—or similar—products, realize that the keen and ill-advised competition which is constantly being encountered is creating unprofitable conditions, and the officers of the companies believe that a merger of all interested companies, coupled with the retirement (from active participation in the conduct of the business) of a number of senior executives who are in receipt of excessive salaries, is the only procedure to adopt.

At a conference of the interested parties, at which the proposal was discussed, you were instructed to outline the accounting procedure to be followed and the financial statements to be submitted by the respective companies.

Prepare the necessary memoranda, embodying therein all the instructions you would issue and the recommendations you would offer, to the end that the accounts of all companies involved may be thoroughly illuminating and may set forth all pertinent facts.

NOTE.—The time devoted to the answer to this question should not exceed forty minutes.

No. 5 (15 points):

"Annual payments made by a corporation under an annuity contract entered into in consideration for the conveyance of realty to the corporation are deductible to the extent that each annual payment is in excess of the present value of such payment at the time the contract was entered into. . . .

"Cost of real estate acquired under an annuity contract is fixed for depreciation purposes as the sum of the present values, at the time the contract was made, of the annuity payments to be made over the life expectancy of the annuitant."

This quotation is the synopsis of an income-tax case recently decided. The vendor was an individual who was expected to live for about twelve years and was to receive equal annual payments in advance during his life. The purchaser was a real-estate corporation.

Using your own figures, which may be approximations, explain and discuss this synopsis.

Examination in Commercial Law

November 14, 1930, 9 a. m. to 12:30 p. m.

Group I

Answer all questions in this group, giving reasons for your answers.

No. 1 (10 points):

In the course of an audit you find that your client has recently purchased improved real estate. He shows you an unexpired fire-insurance policy accurately describing the buildings but payable to the former owner and not assigned or transferred to your client. He says he is fully protected because the buildings are insured and the policy "runs with the property insured." Is his statement correct?

No. 2 (10 points):

On July 7, 1930, a stranger called at the office of Dunham, a public accountant, exhibited the card of a well-known stationery house and obtained an order for analysis paper. On the next day the analysis paper was received by Dunham, together with an invoice payable in 30 days. On July 15, 1930, the stranger called and asked Dunham whether he would pay then for the paper. Dunham paid in cash and the stranger receipted the bill. It developed that the stranger was a solicitor who received a commission on any order accepted and filled, and that he had disappeared without accounting for the collection from Dunham. Can the stationery house collect from Dunham for this paper?

No. 3 (10 points):

Blair, a public accountant, rendered professional services to Jenkins without agreement in advance as to the amount of the fee. Upon completion of the work, Jenkins gave Blair his negotiable promissory note for $2,000 payable 30 days after date, in payment for Blair's services. Two weeks thereafter Jenkins had Blair's work appraised by three disinterested experts, all of whom agreed that the fair value of it was $500. In an action by Blair on this note, can Jenkins successfully defend on the ground of inadequacy of consideration?

No. 4 (10 points):

A corporation had a deficit of $40,000 at January 1, 1929. During that year it earned a net income from all sources amounting to $35,000. In January, 1930, the board of directors declared a dividend of $10,000 out of the 1929 profits. Would this dividend have been legal in your state?

No. 5 (10 points):

Brown, Coates and Danforth were partners sharing profits in proportions of one fourth, one third and five twelfths, respectively. Their business failed and the firm was dissolved. At the time of dissolution no financial adjustments among partners were necessary but the firm's liabilities to creditors exceeded its assets by $24,000. Without contributing any amount toward the payment of the liabilities, Coates moved to Europe, where he was not subject to legal process. Brown and Danforth are financially responsible. How much must each contribute?

Group II

Answer any five of the questions in this group, but no more than five.

No. 6 (10 points):

Curtis, a public accountant, was engaged by Black to make an audit of Black's books, at specified per-diem rates. During the course of this audit, Curtis uncovered a defalcation whereby Black saved $25,000. After the audit was concluded and Curtis had rendered his report, Black promised to pay Curtis an additional fee of $5,000 for uncovering the defalcation. Can Curtis hold Black to this promise?

No. 7 (10 points):

Thompson gave a promissory note, endorsed by Sherwood, to Babcock. This was a demand note for $5,000 with interest at 6 per cent. Later, without Sherwood's knowledge, Babcock made a valid agreement with Thompson reducing the interest rate to 5 per cent. Upon Thompson's failure to pay the note, Sherwood contended that he had been discharged from liability because Babcock had changed Thompson's agreement. Is his contention sound?

No. 8 (10 points):

At 11:30 a. m. Shaw wired Brauer, "Subject prompt reply will engage you to make audit $2,000 fee." Brauer received this wire at 12:16 p. m. At 12:28 p. m. Brauer wired Shaw accepting the offer. At 1 p. m. Shaw had not received Brauer's wire and Shaw wired Brauer revoking his offer. At 1:43 p. m. Shaw received Brauer's wire accepting the offer. Was there a contract?

No. 9 (10 points):

Hughes was a bookkeeper for the Sutton mills, receiving his salary monthly under a contract providing that if he left without giving two weeks' notice he should receive nothing for wages accrued during the current month. On June 14, 1930, Hughes was arrested, convicted and sentenced to jail. The damage to the Sutton mills from want of notice was greater in amount than one half of Hughes' salary for June. Can Hughes recover his salary for the period from June 1st to June 14th?

No. 10 (10 points):

Bishop, a public accountant, desiring to retire from practice, sold all his assets including his goodwill to Palmer for a stated sum. As a part of the sale Bishop covenanted that he would not engage in the public practice of accounting anywhere for a period of ten years. Is this agreement by Bishop valid?

No. 11 (10 points):

C. A. Nimocks was a promoter engaged in effecting the organization of the Times Printing Company. On September 12, 1928, on behalf of the proposed corporation, he made a contract with McArthur for his services as comptroller for the period of one year beginning October 1, 1928. The Times Printing Company was incorporated October 16, 1928, and at that date McArthur commenced his duties as comptroller. No formal action with reference to his employment was taken by the board of directors or by any officer, but all the stockholders, directors and officers knew of the contract made by Nimocks. On December 1, 1928, McArthur was discharged without cause. Has he cause of action against the Times Printing Company?

No. 12 (10 points):

Section 12 of the revenue act of 1928 provides that there shall be no surtax upon a net income of a specified amount; section 25 provides for certain credits against net income; section 22(b) provides that certain items shall be excluded from gross income; section 23 allows certain deductions from gross income. Assume an individual's total income from all sources to be $100,000. Using round amounts to illustrate one or more of the items covered by each of the last three sections listed above, show the computation of his net income subject to normal tax and of his net income subject to surtax (the computation of the tax is not required).

Examination in Accounting Theory and Practice

PART II

NOVEMBER 14, 1930, 1 P. M. TO 6 P. M.

The candidate must answer all the following questions:

No. 1 (30 points):

Following are the balance-sheets of company A and its subsidiaries B and C as at December 31, 1929:

	Companies A	Companies B	Companies C
Assets			
Investments:			
Preferred capital stock of company B—60%	$ 300,000		
Common capital stock of company B—90%	800,000		
Common capital stock of company C—90%	1,300,000		
Bonds of company B at cost	270,000		
Notes receivable—company B	20,000		
Other assets	2,000,000	$2,180,000	$2,000,000
	$4,690,000	$2,180,000	$2,000,000
Liabilities			
Capital stock:			
Preferred—6%	$ 500,000	$ 500,000	$ 500,000
Common	1,100,000	150,000	500,000
	$1,600,000	$ 650,000	$1,000,000
Surplus:			
Balance—January 1, 1929	$1,100,000	$ 150,000	$ 300,000
Net profits for the year 1929	400,000	200,000	300,000
	$1,500,000	$ 350,000	$ 600,000

Dividends deducted	$ 12,000	$ 30,000	$ 30,000
Balance—December 31, 1929	$1,488,000	$ 320,000	$ 570,000
First mtge., 6%, bonds outstanding	$1,000,000	$ 600,000	
Notes receivable discounted—company B	10,000		
Notes payable—company A		20,000	
Other liabilities	592,000	590,000	$ 430,000
	$4,690,000	$2,180,000	$2,000,000

The dividends on the preferred stocks of the respective companies have all been paid during the year 1929.

The bonds of company B, which mature December 31, 1936, were acquired by company A on July 1, 1929, at 90.

Company A acquired its holdings of the stock in companies B and C at the date of their incorporation and has taken up its share of the surplus and earnings of these companies.

From the foregoing, prepare a consolidated balance-sheet as at December 31, 1929, showing surplus at the beginning and end of the year, dividends paid and net profit.

No. 2 (28 points):

The X company formed a new corporation—the Y company—and on January 1, 1930, paid $100,000 for the entire authorized capital stock, viz.: 10,000 shares of no par value (stated value $5 a share).

On the same date the new corporation acquired the business formerly conducted by A and B, for $100,000 in cash. The tangible assets acquired and liabilities assumed as recorded on the books of A and B were as follows: accounts receivable, $25,200; inventory, $9,600; four per cent. bonds, par value, $5,000; land, $15,400; building, less depreciation, $25,000; equipment, less depreciation, $4,300; mortgage payable, $15,000; accounts payable, $25,000.

The building was purchased January 1, 1920; $5,000 of equipment on January 1, 1919, and $6,000 on January 1, 1928. Depreciation is said to have been recorded on a straight-line basis at the following rates: equipment, 10 per cent. per annum; building, 5 per cent. per annum to December 31, 1924, and 2½ per cent. thereafter.

The cash transactions of the Y company for the three months ended March 31, 1930, are summarized as follows:

Receipts

10,000 shares of capital stock	$100,000
Accounts receivable collected	65,000
$3,000 par value of 4% bonds—sold February 28, 1930	2,800
Accrued interest on bonds sold	20
$100,000 par value 5% debentures of Y company due January 31, 1940 (issued January 31, 1930)	90,000
	$257,820

Disbursements

Payment to A and B	$100,000
Merchandise	60,000
Mortgage and accounts payable at January 1, 1930	40,000
Selling, general and administrative expenses	20,000
Life-insurance premium	2,000
Organization expenses	1,500
	$223,500

At March 31, 1930, accounts receivable amounted to $80,000; accounts payable for merchandise $35,000, for expenses $3,000; the inventory was valued at $40,000 and prepaid expenses were computed at $1,000.

According to the directors' minutes, the building and equipment are to be valued for accounting purposes and recorded at cost to A and B, less depreciation on a straight-line basis at 2½% and 10% per annum respectively, and the other assets at the value shown by the books of A and B. Organization expense is to be written off in January, 1930, and depreciation is to be provided on the revised basis stated in the minutes.

Prepare balance-sheet as at March 31, 1930, including provision for federal income tax at 12%, and income account for the three months ended March 31, 1930.

No. 3 (27 points):

The Pine Lumber Company is the owner of a tract of timber, of which it is estimated there will be 1,330,000,000 feet remaining to be cut at January 1, 1931. It intends to cut off this timber and manufacture it over the ensuing ten years, and its present plant, main-line railroad and equipment will be adequate for that purpose with normal replacements.

In the analysis of the accounts for the three years ended June 30, 1930, the following items of expenditure were shown:

New plant extension	$385,750
Plant and main-line railroad replacements	101,070
Equipment replacements	116,480
Construction of logging spurs	217,300
	$820,600

Plant and main-line railroad replacements as above may be considered normal for a three-year period under the usual operating conditions. Equipment replacements may, likewise, be assumed to be normal, but it is to be expected that necessary purchases of new equipment will depend on the number of feet cut.

It is estimated that the construction of logging-railroad spurs into 1,000,000,000 feet of the remaining timber will cost $900,000; spurs already constructed are available for logging 330,000,000 feet.

The company's operations for the three years from June 30, 1927, to June 30, 1930, during which it manufactured 364,000,000 feet of lumber, are summarized as follows:

Net sales of lumber and inventory adjustments		$8,736,000
Cost of sales:		
Logging, manufacturing labor and expense	$6,576,770	
Amortization of logging-railroad spurs	172,900	
Depreciation, plant and main-line railroad	213,500	
Depreciation, equipment	133,910	
Depletion of timber	728,000	7,825,080
Gross profit		$ 910,920
Selling and administrative expenses, taxes, etc.		976,230
Operating loss		$ 65,310
Interest paid		158,850
Net loss for the three-year period		$ 224,160

In order to liquidate all of its present indebtedness, the company is about to negotiate a loan for $1,000,000, to be dated January 1, 1931, with interest at 6 per cent. per annum on the unpaid balance, the principal payable in ten equal annual instalments beginning December 31, 1931.

Using sales prices and expenditures as experienced for the three years to June 30, 1930, as a basis:

Prepare a statement of the "conversion value" of the timber remaining at January 1, 1931, that is, the cash funds to be realized from the operations of the company available for liquidation of the principal under the proposed loan or for other purposes. Calculate the "conversion value" or cash funds to be realized per thousand feet of timber to be cut, to the nearest tenth of a cent.

Prepare also a statement comparing payments to be met in each year under the proposed loan with the cash funds to be available each year, assuming that all the timber will be cut and manufactured in equal annual amounts.

NOTE.—The foregoing relates to the determination of "conversion value" now commonly required by long-term creditors of timber operators, and requires statements other than the orthodox balance-sheet and profit-and-loss statement.

No. 4 (15 points):

You foot the cashbook of the M Manufacturing Company for October, 1930, reconcile the bank accounts as at the close of business on October 31, 1930, and list the cash and cash items on hand at the beginning of business the following morning, with results as follows:

Cash in bank and on hand at close of business on October 31, 1930, including office cash fund of $3,500, ascertained as follows:	
Balance as at September 30, 1930	$ 26,250.25
Receipts for October	179,750.00
	$206,000.25
Payments during October	174,311.42
Balance as at October 31, 1930, per cashbook	$ 31,688 83
Bank balances, as reconciled:	
First National Bank, Blankville	$ 21,413.28
Downtown Trust Company	5,260.10
Downtown Trust Company—Payroll account	1,515.45
Cash and cash items on hand:	
Cash	1,189.32
*Receipt of mail clerk for postage fund	25.00
*Receipt of shipping clerk for expressage fund	10.00
Unentered vouchers for sundry payments made in cash	504.87
I. O. U.'s for payroll advances (approved by factory manager)	213.43
Cheque dated September 15, 1930, cashed for purchasing agent, returned by bank September 22, 1930, "account insufficient funds"; purchasing agent has promised to "make good"	100.00

*Assume that these funds were checked later on the same day and found to be in order.

Cheque of cashier, dated October 31, 1930, which he states was to cover cash withdrawn by him for personal use.....	$ 50.00
Unentered cheque from the Transylvania Railway Co., dated October 20, 1930, which, according to the covering letter in the files, was received October 22, 1930, and relates to a claim filed by the M Manufacturing Company under date of June 9, 1930..................................	124.65
Cheque of Green & Co. for bill of M Manufacturing Company, dated September 20, 1930, returned by bank October 31, 1930, account payment having been stopped by Green & Co...	358.95
Undeposited cheques from customers, as follow:	
Clark & Son, dated September 22, 1930, entered in cashbook September 24, 1930..........................	287.50
Jackson & Bro., dated September 22, 1930, entered in cashbook September 24, 1930......................	240.75
Miller & King, dated September 26, 1930, entered in cashbook September 29, 1930..........................	394.60
Thompson Stores, Inc., dated September 29, 1930, to be entered in cashbook as of November 1, 1930..........	150.30
Retail-stores collections to noon, October 31, 1930, to be deposited and entered in cashbook as of November 1, 1930..	211.45

Consider the propriety of the foregoing items and list any that you would be prepared to exclude in ascertaining the actual status of the cash account. Give reason for exclusion in each case.