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Editorial

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EDITORIAL

Eyes Front

One of the most remarkable and heartening features of the difficult times through which the world has been passing has been the good sportsmanship of almost everyone in this country and in many other countries as well. It has been particularly noticeable here because the people as a whole have probably suffered a greater drop than anywhere else. They were so excessively prosperous up to the middle of 1929 and there has been such deep depression since that the distance between the heights and the depths has been appalling. Yet in spite of the sudden transition from affluence to penury there has been very little complaining and almost no whining at all. One reads a good deal of comment here and there upon the sporting way in which the well-to-do have taken their beating and there is no doubt that they deserve the highest praise. It is not a comfortable experience to pass from the lap of luxury to the grip of want, and there might be a good deal of justification for anyone who became sorry for himself. But self-pity is a contemptible thing and the people seem to know that. They have made up their minds that it is all in the day's march, all part of the general scheme of things, that one should go from high to low and while in the low hope again for the high. The new poor, to use a most expressive English phrase, are acting very well in their poverty. People who never dreamt that they would be compelled to think of the dollars have learned to compute the cents, and some of them seem to be having a rather good time doing it. There is, of course, a certain amount of acting

in all this. Most of us like to present a bold front to the enemy, but it is not uncommon to hear men, and women too, speaking quite frankly and saying that they are really enjoying getting to work and finding that a dollar does mean something. It is rather good fun they say, some of them, to see how much a dollar can be made to do. There are innumerable men who now find themselves back where they were fifteen, twenty or twenty-five years ago and they are faced with the necessity of starting afresh; and the splendid thing about it is that they are doing what has to be done and for the most part doing it cheerily.

Good Soldiers All But there is another and more important aspect of the case which has not received as much comment as it deserves. One does not read encomia of the wage-earning folk for their acceptance of hard times. Some of them are suffering severely. Nearly all of them receive less actual compensation for their labor, although the value of the compensation is at least as great as it was, but there are millions of toilers who are compelled to labor in part time and to whom the enforced idleness is a serious burden, yet one can say truly that there has been very little protest. Of course, there has been a good deal of what might be called organized complaint, but the individual workers, in this country at least, have gone down into the depression with something like a song upon their lips. They seem to realize that for years they have been the most fortunate representatives of their class in all the world and, now that the general conditions prevent the continuance of that prosperity, they, like the well-to-do, are taking their medicine with a smile. It is impossible to speak too warmly in laudation of the attitude of all classes of the community, from the highest to the lowest. Here and there a labor leader, intent upon maintaining a job for himself, has been indulging in the usual sort of class oratory, and we have heard echoes of half-hearted threats; but these things were to be expected. A good many labor leaders have never done anything for humanity except to make a noise. And the laboring men and women are not following the so-called leaders as they did. In a great many of the trades and industries they have learned to think for themselves. If one desires to find the benefits of depression he may discover that one of them well worth while has been the good sportsmanship of both capital and labor. If one mingles with tradesmen, artisans or even the men

who depend solely upon physical labor for their livelihoods, he will find among them all the same noble spirit of acceptance. It is enough to make every American prouder than ever of his country to see how Americans can act in the face of disaster. With such a spirit abroad among us there can be no doubt whatever about the ability of America to carry on, and the same thing can be said of many of the other nations. Great Britain, France and others are presenting a record of courage and cheerfulness on the part of the people which deserves the permanent gratitude of the race. The trial has been long and severe. It is many a day since there was so protracted a period of distress. There have been other crises which have been more acute, but this one is notable for its long continuance. It is, therefore, a greater trial to most people than were the short, sharp depressions of the past—yet, in spite of that also, the people carry on.

**Railways and
Audits**

In the notice of the annual meeting of the Atchison, Topeka and Santa Fé Railway Company, to be held at Topeka April 28th, it is announced that there will be a vote upon a proposal to amend article XVIII of the by-laws of the company, which reads thus:

“The stockholders at each annual meeting shall elect an independent auditor or firm of auditors to audit the books and accounts of the company as soon as may be after the close of the fiscal year. The certificate of such independent auditor or auditors shall be published in the annual report of the company.”

The notice of the meeting is accompanied by a letter from the president of the company to the stockholders and the following paragraph from that letter is significant:

“The proposed amendment of article XVIII of the by-laws is for the purpose of eliminating therefrom the compulsory requirement that there be an annual independent audit of the company’s books and records. The company’s books and records are kept in the manner and form prescribed by the interstate commerce commission and are annually inspected by representatives of the interstate commerce commission and of the commissioner of internal revenue. Most of the larger railroad companies no longer have independent audits; such audit is, therefore, believed to be a needless expense.”

In a sense the action which will doubtless be taken by the stockholders of the Atchison, Topeka and Santa Fé Railway Company

marks a stage in the development of accounting practice, but it can not be said that it marks progress toward better conditions or frank exposition of affairs. It is perfectly true, as Mr. Storey says in his letter, that most of the larger railway companies have given up the custom of independent audit. He might also have said that at no time in the history of American business has there been any general inclination on the part of railways to submit their records to analysis by independent auditors. Many of the great trunk lines and some of the minor roads have employed auditors in the past, but with very few exceptions the scope of audit laid down by the company—or it would be more accurate to say by the directors of the company—has not been sufficiently comprehensive to permit a searching investigation of all constituent factors.

History of Railway Audits

In the early days, much of the capital invested in American railways came from Great Britain, and British accountants were engaged to come to America for the purpose of safeguarding British interests. The ventures in which foreign money was most generously employed were the railways, and, accordingly, the audit of the larger roads was for a long time conducted by men who had been retained by British investors. The nature of the audit which was common in those times differed somewhat from the modern idea of thorough analysis. Many things which the auditors might have desired to do were not possible within the limited scope allowed them, and there was some dissatisfaction on the part of accountants because of the restrictions which were placed about their operations. To the railways it may have seemed that the kind of audit which was customary did not justify the expense, especially in view of the increasing supervision exercised by the interstate commerce commission. If it had been considered possible by the railways to employ accountants to make thorough investigation of all the activities of the railways, the tendency to disparage independent audit, indicated in the letter of the president of the Santa Fé, would never have gained headway. Probably there is not a well informed railway man in the country who would deny the advantages of real analysis of accounts, records, etc. and of inspection of conditions, but the unfortunate fact is that the railways began their association with independent audit by calling for incomplete investigation, and,

consequently, the custom of audit has become less and less common—and now the announcement of a proposal by the Santa Fé to abandon the principle of audit removes one of the last important traces of an earlier method of supervision.

Is Government Supervision Sufficient?

If one looks at this subject from the point of view of the management, the action of the railways in giving up independent audit may seem reasonable, but there is a distinct peril in the change. It is true enough, as the president of the Santa Fé says, that the accounts of railways are inspected by representatives of the interstate commerce commission and the commissioner of internal revenue, but this is really confusing the question. Audit by agents of the interstate commerce commission is directed largely toward the review of methods of account-keeping and the observance of rules and regulations. Emissaries of the bureau of internal revenue conduct an audit solely with reference to the incidence and collection of taxes. Audits by public accountants are for the benefit of stockholders, and in nine cases out of ten they would be wholly different from the kind of audits conducted by either of the government departments which have been mentioned. Furthermore, it may be permissible to inquire how searching government inspection can be. Representatives of government may not be careless, but inspections of all kinds made by servants of federal, state or municipal governments are not, as a rule, adequate. It is rather notorious that bank examinations, for example, in some states mean almost nothing. If bank examinations were always what they should be, many of the banks which have failed in the last year would not have been allowed to remain so long with open doors and receiving tellers on duty, and countless millions of depositors' money would have been saved. It stands to reason that no inspector, accompanied perhaps by a helper or two, can stop for two or three days and review the accounts of a bank of any magnitude and give a certificate of condition which carries much weight. In the case of public utilities, which in every state are supervised by commissions of one sort or another, the extent of investigation is quite restricted and it is commonly believed that fatal weaknesses in the structure of such corporations could exist without attracting the attention of the casual inspector. It is true throughout the world that civil servants are

always in danger of becoming mechanical and perhaps too much addicted to rule of thumb. It is probably safe to say that the discreet investor would not care to rely solely upon opinions expressed or approvals given by investigators employed by government, whether federal, state or municipal.

**Railways in a Class
by Themselves**

But the great point to be remembered in this whole discussion is that even in the case of railways, which perhaps present as much difficulty as any department of industry where the question of audit is involved, it is dangerous to relinquish the examination and report by unbiased investigators. Perhaps the tendency which Mr. Storey recalls is due primarily to a desire to cut down expenses. In the case of the Sante Fé, which is one of the best managed roads in the world, such an argument would not be favored. It is the history of that road that the outlay of money and effort for the betterment of conditions and the prevention of decline in standards has never been withheld. Some weaker roads may, however, have been short-sighted and have regarded the employment of professional accountants as an act of needless expense, to use Mr. Storey's own words. Furthermore, it would be a grave mistake to regard railways and ordinary kinds of business in the same light. However weak may be the arguments of the railways which advocate doing away with audit, they would appear strong in comparison with anything that could be adduced to suggest avoidance of audit in other kinds of activity. We do not have much faith in the efficacy of what may be called official audit, by which we mean investigations or inspections conducted by officers of the government, but whatever protection may be afforded by the labor of such agencies is wholly lacking in the case of ordinary industry and business. The accountants who have been distressed by the letter of the president of the Santa Fé really need feel no grave misgiving. The case is one that is not controlling and it would not be astonishing to find that in the course of a year or two there will be a reversion of feeling and accountants will be called in again, this time to perform a complete audit of railway accounts and activities.

Omnium Gatherum Our attention has been directed to the third annual report of the First Bank Stock Corporation, Inc., in the state of Minnesota. In the course

of this report mention is made of the First Service Corporation. And, as this does not seem to be the kind of an organization one usually associates with the conception of banking, it is necessary to turn to the articles of incorporation to find out what it may be. The following is an extract from the certificate of incorporation:

General Nature of Business

(a) To conduct researches into and investigations of any and all businesses and business methods and to disseminate the results of such researches and investigations and to give information and advice to banks, trust companies, financial and other corporations;

(b) To furnish a statistical service of whatsoever nature for corporations, partnerships and individuals;

(c) To keep, examine, audit, analyze, report upon, and certify to the books, accounts and records of corporations, partnerships, and individuals, to install systems of accounting and to transact a general auditing and accounting business, all in such manner and to such extent as may be permitted by law;

(d) To engage in the business of credit reporting, to collect and disseminate credit information, and to install credit systems;

(e) To buy, sell, deal in, and do a general brokerage business in all kinds of listed and unlisted stocks, bonds and other securities;

(f) To act directly or indirectly as agent for insurance, indemnity, and surety companies in soliciting and receiving applications for insurance policies and indemnity and surety bonds of every description, to collect premiums, and to do such other business as may be delegated to agents by such insurance, indemnity, and surety companies, and to conduct a general insurance and indemnity and surety bond agency and an insurance and indemnity and surety bond brokerage business;

(g) To conduct the business of an agent in the collection, adjustment, compromise, and settlement of debts, demands, accounts and claims of all kinds;

(h) To conduct a general advertising business, both as principals and agents, including the preparation and arrangement of advertisements and the manufacture and construction of advertising devices and novelties, to erect, construct, purchase, lease, or otherwise acquire, fences, billboards, signboards, buildings, and other structures suitable for advertising purposes, to carry on the business of printers, publishers, painters, and decorators in connection with such advertising business, and to make and carry out contracts of every description in connection therewith;

(i) To examine into the assets, business and business prospects of corporations, partnerships, and individuals, and to make reports thereon and recommendations as to the value of any such business and the future prospects thereof;

(j) To appraise real estate, securities and other property and to report upon such appraisals;

(k) To furnish information and advice with reference to income and other taxes in such manner and to such extent as may be permitted by law;

(l) To purchase, lease, manufacture, or otherwise acquire, hold, sell, exchange, repair, maintain, improve, mortgage, and in any other manner deal in and deal with office supplies and furniture and fixtures of every description;

(m) To purchase, lease, or otherwise take, hold, sell, exchange, transfer, repair, maintain, improve, mortgage, and in any other manner deal in and deal with real property, mixed, and personal property wherever situated;

(n) To manage and operate as agent for corporations, partnerships, and individuals, farms, farm lands, and buildings and real estate of every description, rural or urban, wherever situated;

(o) To purchase or otherwise acquire, hold, use, sell, and in any manner dispose of and deal in patents, inventions, improvements, processes, copyrighted publications, trade-marks, trade names, rights and licenses secured under letters patent, copyrights or otherwise, and to grant licenses or other rights therein.

Cash, or What
Have You?

There may be something significant in the fact that the categories of undertakings end on the letter "o", but one must confess to a sense of disappointment that the list is not quite complete. Two or three things seem to have been omitted. For example, nothing is said about the establishment of a crèche—yet it would hold great possibilities. One might imagine lines of depositors placing their wards in safe keeping while they wandered from branch to branch of this all-inclusive organization. It might be profitable in many ways. It has been suggested that perhaps the articles of incorporation were written by some young lawyer with an expansive imagination, who thought to protect his clients in any extravagant ventures which their energies might involve. A great many articles of incorporation attempt to swallow the world. Then again it may be that the directors have not had an opportunity to consider the full force and effect of this all-embracing incorporation. Some of them are men of prominence in the community, and it is difficult to understand how they could be acting as directors without knowledge of the facts, but it is permissible at least to give them credit for such a possibility. Perhaps the real purpose of this new company is to enter into the field of accounting. If so, it has an unhappy future ahead of it. Some years ago a few banks, notably in Detroit, made the essay of penetration into the realms of public accounting, but it did not pay. It was generally condemned, and, so far as we know, the plan has been entirely abandoned. There have been other instances of men who were not accountants attempting to break into the field of accountancy, but the result has always been failure in the long run. It is generally a pretty good plan for the cobbler to stick to his last and the banker to stick to his bank. Brokers, analysts, credit agencies, insurance companies, advertising agents, appraisers, furniture dealers, real-estate men, patent attorneys, lawyers, accountants—these are some of the enemies that will be aroused by the attempt of a bank to do everything. The fate of Æsop's frog awaits such self-inflation. No one can possibly expect success who attempts to do everything. There is probably nothing in the laws of Minnesota to preclude embarkation upon a wholesale adventure of this sort. But what would the federal reserve board say about so elastic a policy of one of its members? The answer to that question should be interesting. If the directors do not know about the possible activities of this

new corporation they should be grateful to any one who will bring the matter to their attention. For example, in the list of directors we find presidents of insurance companies, presidents of cereal-producing companies, railway presidents, presidents of copper companies and packing companies, etc. Would the president of an insurance company, for example, be in favor of an extension of the First Service Corporation's activities to include insurance? Yet that is one of the things which is specifically permitted in the articles of incorporation. The matter would not be worth consideration for a moment were it not for the prominence of some of the men concerned, but in any case it is preposterous and if the directors have a sense of humor they will be greatly entertained by reading over those items from "a" to "o" inclusive.

**A Lucid Statement
of Condition**

In the report of the president of the International Harvester Company to the stockholders relative to the condition of the company at the end of the fiscal year ended December 31, 1931, there is interesting evidence of the increasing trend toward frank and clear statements of condition. For example, the income account shows profit for the year amounting to \$1,346,537 and to this is added \$11,000,000 taken from reserves from prior years' earnings for decline in market values, etc., now released to income. The balance carried to surplus is therefore \$12,346,537. In the remarks attached to the report this disposition of reserves is the subject of comment as follows:

"Reserves established in prior years for the protection of the business in adverse times were drawn upon to the extent of \$11,000,000, thus limiting the call upon surplus account to \$4,412,000, for the payment of dividends declared in 1931. The remaining reserves are believed to be sufficient to meet any adverse conditions that may be reasonably anticipated."

The certificate of the auditors is one that appeals to the common-sense of the ordinary investor. In a great many cases there has been just criticism of the vague generalities of accountants' certificates, but everyone who understands the simplest principles of business will feel a sense of confidence in such a statement as that which is attached to the accounts in this case.

Reports of Condition

In former issues of THE JOURNAL OF ACCOUNTANCY we have drawn attention to the efforts being made by the authorities of the New York

stock exchange to encourage the presentation of more frequent reports of condition from the companies listed on the exchange. A statement in the New York *Evening World-Telegram* on February 25th contains a tabulation showing the frequency of earnings statements of listed companies. From this it appears that 23.6 per cent of these corporations submit annual reports, 21.4 per cent, semi-annual, 51.7 per cent, quarterly and 3.3 per cent, monthly reports. Practically all the reports in the last category are those of public utilities. The statement also informs us that only thirteen concerns failed to live up to their agreement with the stock exchange with reference to the frequency of reports. Of the thirteen, six are in receivership. This is an excellent record and indicates that the efforts of the exchange are bearing fruit. It seems that nothing but good can result from the submission of frequent reports of condition.

Send Us Clients

A midwestern newspaper recently contained an advertisement which read as follows: "Accountant wants any kind of accounting clientele." This advertisement was sent to us with the intention of drawing a moral, but it seems to be about as frank and complete an advertisement as one could imagine. It may be that the person who inserted it is in peculiar need of clients, but at least he is forthright. If every professional man, whether physician, lawyer, accountant or other, were asked a plain statement of fact he would admit that his wants were parallel to those of the young gentleman who advertised. The only difference is in the manner of approach. One may be a bit skeptical, however, about the efficacy of this cry from Macedonia.