

4-1935

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Recommended Citation

Kress, W. J. B. (1935) "Accounts of a Cigar Manufacturer," *Journal of Accountancy*. Vol. 59 : Iss. 4 , Article 3.

Available at: <https://egrove.olemiss.edu/jofa/vol59/iss4/3>

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Accounts of a Cigar Manufacturer

By W. J. B. KRESS

Cigar manufacturers in this country operate under the jurisdiction of the collector of internal revenue, with their activities limited to the production and sale of cigars. They must comply with all provisions of the laws governing the manufacture and sale of cigars, and their factories are under inspection of government agents.

Cigar factories range from the small factory, where the owner is the sole operator and makes cigars by hand, to the huge plant employing a thousand or more operators making cigars either entirely by hand or with the aid of machines.

Most of the larger factories are in cities and towns where cheap labor is available, and they employ women chiefly. If the plant is in a big city, it will usually be near the homes of the people who form the working force. These conditions have a tendency to lower the labor cost, which forms a fairly large part of the cost of cigars.

For present purposes, a cigar factory using modern machinery and employing several hundred operators is taken as a model. I shall confine myself wholly to the manufacture of the cigar and shall not attempt to discuss the growth and cure of tobacco from which the cigar is made. Some cigar manufacturers grow and cure their own tobacco, or purchase it direct from the growers and cure it themselves, but most of them purchase it already cured. The growing and curing of tobacco is considered an industry by itself. The processes involved differ entirely from those of cigar manufacturing.

ORGANIZATION

The factory departments consist of the warehouse, tobacco (casing, stripping, blending and assorting) rolling and packing.

At the head of the entire organization is the president and general manager. He usually does the purchasing of all tobacco, after testing samples of it, as to yield, quality and "burn." The secretary-treasurer, the sales manager and the factory superintendent are directly under the president's supervision.

All sales activities are in charge of the sales manager, who generally is an officer of the company. The superintendent is held responsible for the control and execution of production, and the foremen are answerable to him for the work performed in their departments.

FACTORY AND WAREHOUSE FACILITIES

The factory buildings should be large enough to take care of all departments without overcrowding. They must be well ventilated, so that the moisture in the air will remain fairly constant from day to day. This is of great importance, as tobacco is extremely sensitive to weather. The various operating departments should be so arranged in the building that no unnecessary time or handling is required in passing the product from one process to another.

A warehouse for the storage of domestic tobacco or imported tobacco upon which duty has been paid and a bonded warehouse for imported tobacco on which no duty has yet been paid, both of ample size, are required for storing the large quantity purchased from time to time. Some manufacturers have a year's supply, or even more, of tobacco on hand at one time. The advantage of having a bonded warehouse is obvious—a great quantity of imported tobacco may be purchased and carried on hand in custody of the government, while the duty payments may be deferred until the tobacco is needed.

Tobacco is stored in the warehouse according to size, quality and grade and is so arranged that no unnecessary handling is required when any certain kind has to be taken out. Finished cigars are stored in specially built humidors, so that they may not be affected by weather conditions.

RAW MATERIALS

In the manufacture of cigars, leaf tobacco is the raw material. It is the highest grade of tobacco produced, and is quite different from that used for pipe smoking or cigarettes. It is grown in different soils, in different localities and under different conditions. Leaf tobacco may be divided into three classes:

- (1) Wrapper leaf—the outer covering of a cigar and in leaf form.
- (2) Binder leaf—the inner covering of a cigar and in leaf form.
- (3) Filler—that which constitutes the bulk of a cigar and may be either leaf or scrap from leaves.

Each of the above classes may consist of tobacco known as Havana, broadleaf, Connecticut shade grown, Sumatra, Java or Porto Rico. The highest grades of each are used for wrapper purposes, the lower grades for binder and filler purposes.

The most expensive cigars are made of the highest grade wrapper and binder, free of holes, with the filler of uniform length and quality and so arranged that the cigar will draw and burn evenly throughout.

MANUFACTURING PROCESSES

The operations involved in the manufacture of a cigar, in their sequence, may be classified as follows:

Preparation of tobacco:

Casing

Stripping

Blending

Assorting wrappers and binders

Making of cigar:

Bunching

Wrapping

Examining

Packing:

Shading

Pressing

Banding

Cellophaning or tinfoiling

Tobacco is received in bales or cases in rather dry and brittle form. To make it more pliable, the leaves are moistened with water, and this operation is called "casing." The process of casing starts before the tobacco is unpacked. The tobacco, in the original bale or case, is put in a sweating room or humidior to absorb a certain amount of moisture so that the leaves will not break or crack while being unpacked. The leaves, which come packed in bunches, are shaken apart, dipped in water and then set on racks for the water to become absorbed or to evaporate. The bunches are left on the racks for several hours, during which they are moved three or four times so that all leaves may become evenly moistened. The tobacco is then ready for stripping.

Stripping, or stemming as it is sometimes called, consists of removing the mid-rib from the tobacco leaf. This operation may be done by hand, but it is generally performed with a machine

having two rotating circular knives. The leaf is fed into the machine in such a way that its vein passes between the knives and is cut out.

After being stripped, the wrapper and binder tobaccos are turned over to selectors who make the proper selections as to size, texture and quality for the cigars which are to be made at the time.

The next process is "blending," which is the mixing of the proper quantity and grades of various kinds of filler tobacco for the purpose of producing certain blends for the different sizes and grades of cigars.

The wrappers and binders, in their moistened state, and the filler, in a somewhat drier state, are then delivered to the rolling room, where they are rolled into cigars.

The first operation in the actual making of a cigar is "bunching." An operator takes a binder leaf, lays the proper amount of filler tobacco within it, and rolls the whole into cigar form, the binder forming a sort of rough wrapper. The roll is then placed in a cigar-shaped groove in a mould, which is a wooden block generally containing fifteen grooves. When the mould is filled, a duplicate block is placed on top and the whole mould is put into a hand press, where it is left for several minutes to allow the "roll" to form itself perfectly.

Wrapping is the next operation. This consists of taking the "roll" of tobacco out of the mould, trimming it to the right size, with the aid of a gauge, rolling a deftly cut wrapper around it and fastening the end of the wrapper with gum tragacanth. The cigars are then handed over to inspectors who examine them as to size, workmanship, etc. This is the procedure in the hand method of making a cigar, with all operations done by one operator.

In large factories, and even in some of the smaller factories the bunching is performed by one operator and the wrapping by another. The bunching may be performed with mechanical aid. With an improved bunching machine, one operator feeds the filler into the machine and a second operator places the binder in place to receive the filler. Where a more simple contrivance is used, which is much slower, one operator handles both filler and binder. In both cases the binder is rolled around the filler mechanically.

In the all-machine-made method, one machine performs all the operations in the same order. The method of making is identical,

the machine simply doing some of the work the hand otherwise would do. Four operators, however, are required on each machine. The first one puts the filler in the proper place, the second and third put the binder and wrapper respectively in place, and the fourth examines the cigar and places it in a container.

The order in which the packing operations are performed depends upon whether the cigars are cellophaned or tinfoiled. If cellophaned, the operations in sequence are shading, pressing, banding, cellophaning, packing. When tinfoiled, the shading operation may be eliminated and the banding may be done after the tinfoiling.

In shading, the cigars are selected and grouped as to color and general appearance. The cigars in each group are as nearly uniform as possible. They are put into a box and pressed, for the purpose of giving them certain shapes. Banding is done by machine and consists of putting the paper band (usually with the brand inscribed on it) around the cigar. Cellophaning and tinfoiling are machine operations.

As a rule the labeling, etc., of cigar boxes is performed by the maker of the box, with labels furnished him by the cigar factory.

MATERIAL RECORDS

The material records in general use in a cigar factory are:

Purchasing:

Purchase requisition

Purchase contract or order

Receiving:

Report of material received

Invoices from creditors

Storing:

Stock records

Issuing and disposing:

Material requisition

Interdepartmental material reports

The purchase requisition is a request for purchases, prepared by general manager, head of office department, factory superintendent or foremen of operating departments, according to their requirements. The purchase contract or order is a form upon which are entered definite agreements with and instructions to the vendor as to quantity and kind of material or supplies required. Both the requisition and purchase contract or order are

prepared in duplicate. The original is sent to the person in charge of purchases, and the duplicate is kept by the department in which it originated. The original of the purchase contract or order goes to the selling company, and the duplicate is kept on file. The purchase contracts or orders are filed either alphabetically, according to names of concerns to which they are sent, or according to nature of material ordered so as to facilitate ready reference for checking.

The report of material received records the date of receipt, the quantity and complete description of the material and the name of the concern from which it is received. This report is filled in by the receiving clerk after count and inspection of the material received and is then sent to the office for checking purposes. The invoices from creditors are checked with the purchase and receiving records, price records, etc., for verification of charge and then passed for entry upon the general and cost records.

Separate records are kept for the tobacco, other material and supplies and finished cigar stock, and these records are so arranged that they provide data for the "perpetual" inventory. The tobacco record, which may be in either loose-leaf or loose-card form, covers all the tobacco purchased and all the withdrawals for production. It is divided into sections for segregation of tobacco in vendor's possession, in bond and in company's warehouse or factory, each section being subdivided into kinds and grades of tobacco. The "other materials and supplies" record covers the purchase and withdrawal of such items as boxes, labels, bands, tinfoil, cellophane, machine parts, supplies, etc. The finished cigar record is arranged to show the number and value of cigars in each brand and size and whether they are stamped or unstamped.

The material requisition is an approved order by a department head or foreman authorizing the issuance of tobacco or other material and supplies needed for a particular purpose. The interdepartmental reports are daily records prepared by the various departments showing the weight, kind and grade of tobacco and its use, delivered from one department to another, and the number of cigars produced and packed.

In addition the company keeps a book conforming with requirements of the United States internal-revenue department. In this book there must be a daily record of all unstemmed or stemmed leaf tobacco, cuttings, clippings, scraps and stems re-

ceived at the factory, and of all such articles removed therefrom; the number of cigars manufactured and removed, tax paid, or used by employees; revenue stamps of each class purchased and used; also the number of cigars, stamped and unstamped, separately and value of attached and unattached stamps of each class on hand before the beginning of business on the first day of each month—to be ascertained by actual inventory. A monthly abstract from this book must be furnished to the collector of internal revenue before the tenth day of each month.

Tobacco is usually received in bales or cases, which are numbered, and the grade, quality and weight of the contents are noted thereon. Upon receipt, an entry is made in the tobacco record under the proper classification. Tobacco purchased, but held by the vendors until shipment is requested, is charged to the vendors in the tobacco records and when received is transferred to stock in hand. All supplies when received are entered in the supplies record. Both tobacco and supplies are issued on requisition when needed for production, and the proper entries are made in the various records. The finished product is recorded in the finished-cigar record, according to brand, size, etc., and, when the cigars have been sold and shipped, the records are credited accordingly.

As a general rule, comparatively little time and labor are required in taking a physical inventory, as the commodities are not numerous. For tobacco in stores, the weight marked on an unbroken bale or case is taken as being correct. When the bale is broken, the amount is determined by actual weight. The work in process consists of loose tobacco in various stages of preparation and the loose cigars in the various stages of packing. Tobacco in process is taken at actual weight, while the loose cigars and the finished cigars (packed) are taken by count. Tobacco in hands of vendors or in bond is taken from the store's record.

The taking of inventory is usually under the supervision of a financial officer of the company. Department foremen are delegated to supervise the actual count in their departments and the recording on inventory sheets. After the recording has been done, the sheets are summarized, according to desired classifications, and are turned over to the cost or accounting department for valuation, extensions and for checking quantities against perpetual inventory records. Cost value, as shown by the material stock and cost records, as a rule is used for pricing.

In this industry the piece-work plan of wage payment prevails. All productive labor, with the exception of casing and wrapper stripping, is paid at an established rate per thousand cigars or per pound of tobacco. Casing and wrapper stripping labor is on an hourly rate basis, because it has been found that this method leads to more careful handling of the tobacco. Non-productive labor—that which can not be applied directly to an operation—is on a time-unit basis.

In addition to the piece-rate, some manufacturers pay various bonuses for production over a certain amount and premiums for getting more wrappers out of a given amount of tobacco. Learners are put on piece-rate as soon as they become proficient. In factories where moulds and machines are in use, the employees work in teams of two or more, wherever possible.

Employees on the hourly-rate basis are furnished clock cards on which their working time is recorded. Employees on piece-rate are given piece-work cards, on which the time, quantity and nature of product are recorded daily. In order to facilitate payroll analysis, a differently colored piece-work card is used for each operation. Space is provided on the cards to show number of hours worked, quantity produced, rate and total pay.

At the end of the weekly payroll period, all cards are collected and the amount of each person's pay is calculated and extended, according to the rates shown in the permanent rate book. A payroll sheet is then prepared from the cards and is signed by the superintendent. An analysis of the payroll is made to ascertain the productive and non-productive labor in each department and a further analysis of the productive labor to ascertain the amount of labor applicable to each brand of cigar. The analysis is compared with the payroll sheet, after which payment is made from the latter by cash or cheque.

Payroll calculations can be verified in the aggregate, in many instances, by taking the total production for the period and multiplying it by the established rate per operation. In many cases production in one department can be checked quite readily with the production in another department. Salaries of officers, office employees and factory superintendent are kept in a separate record and are paid semi-monthly.

Tobacco is transferred from stores to the tobacco department only upon requisition. The requisition shows the date issued, grade and class of tobacco, weight, case or bale number and the

purpose for which the tobacco is to be used. Upon receipt of the tobacco by the tobacco department, a tag, having upon it the same information as the requisition, is attached to the lot. For identification purposes this tag accompanies the lot through every process. When the tobacco goes through the stripping process, another tag is attached showing the stripped weight and the loss through stripping. Deliveries are made to the rolling room from the various lots as requirements demand, each delivery reported by weight and description of tobacco. The numbers of cigars made are reported in units of one thousand.

After all the tobacco in a given lot has been delivered to the rolling room, the tag that accompanied it is returned to the office. Reports of the daily production in each department are also sent to the office. During the month, the production reports are compared with the tags and with the reports from one department with another. The reports are then analyzed as to brands, and at the end of the month a summary is prepared. This summary forms the basis for calculation of the cost of tobacco consumed.

Each brand of cigar has been allotted a predetermined unit weight for tobacco. By maintaining the identity of the tobacco until it is made into cigars, the actual amount of tobacco consumed for any brand can be readily compared with the predetermined weight by dividing the consumption by the production.

The principal item of the material cost is tobacco. Other items which form part of the cost are boxes, labels, bands, cellophane, tinfoil, etc. For all material, other than tobacco, the actual invoice price is used as a basis of cost.

In the case of tobacco, the basis of cost is the purchase weight, invoice price, plus freight and import duty. This cost price, however, is adjusted by the amount applicable to loss through stripping, as all tobacco consumption is finally calculated on stripped weight. The adjusted price per pound is found by taking the purchase weight of the tobacco consumed, multiplying it by the invoice cost price, subtracting therefrom the proceeds from sale of scrap, stems and cuttings, and dividing the resultant amount by the actual weight after stripping.

Labor costs are divided between productive and unproductive charges. Productive labor consists of the wages paid for casing, stripping, blending, bunching, rolling, shading, foiling, banding,

etc. The cost of each operation is a fixed rate per unit, with the exception of casing and wrapper stripping, the unit cost of which is found by dividing the total labor for these operations by the total production. If a bonus or premium be paid, it is added to the labor for the operation to which it applies, and the labor is then divided by the total production. When a brand of cigars is made by hand and by machine at the same time, the labor applicable to both is spread over the combined production. Unproductive labor includes wages paid to warehouse employees, foremen, examiners, machinists, etc. Productive labor is charged direct, but unproductive is charged to appropriate burden accounts and subsequently redistributed.

Entries for material consumed are based on requisitions on the stores and entries for labor on the payroll analysis sheet. After the cost of tobacco consumed has been determined, 1,000 cigars are used as a unit basis for costing.

Another item that enters into the factory cost of cigars is the cost of the revenue stamps that must be affixed to containers in which cigars are packed.

The principal items of overhead expense ordinarily found in the cigar industry are:

- Indirect labor
- Salaries of foremen and superintendent
- Factory and warehouse rental
- Machine rentals and royalties
- Insurance and taxes
- Repairs and renewals
- Heat, light, power and water
- Factory supplies
- Depreciation

The distribution of overhead to the various makes of cigars on a unit basis of 1,000 has been found to be the most convenient. The proportion of overhead applicable to machine-made and hand-made products will differ, but, as the identity of each make is lost after leaving the rolling department, the production as a whole is taken for basis of distribution. For information as to relative costs for each method of manufacture, however, the expenses are analyzed and appropriately applied.

Depreciation is computed on a straight-line method—that is, uniform amounts are set aside periodically. The basis is the original cost, which not only includes the purchase price but also

the freight and expense of installation. The rates in general use follow:

	Per cent.
Buildings.....	2 to 5
Moulds.....	12½ to 20
Machinery and equipment.....	10 to 12½
Office furniture and fixtures.....	10 to 12½
Delivery equipment.....	25 to 33½

The moulds are subject to obsolescence more than to wear and tear through use, because of changes in the size and shape of cigars. This accounts for the fairly high depreciation rate.

All banding machines and cigar machines are leased by the cigar factories, as they can not be purchased outright from manufacturers. The machines are leased on a stipulated monthly rental or on royalty upon production. In addition to the monthly rental for cigar machines a substantial initial payment is made. This payment is amortized over the period of the machine lease.

Where a detailed plant ledger is maintained, the depreciation charged off is entered in detail so that the exact residual value of the asset may be determined at any time.

Plant renewals are charged direct to the appropriate asset accounts. Repairs to plant and equipment are charged to an expense account, unless the repair materially prolongs the life of the asset, and in that case repairs are charged against depreciation reserve.

Marketing of the company's various brands of cigars is accomplished by the sales department. The personnel of this department consists of the sales manager, salesmen, advertising department, shipping department, statistical and file clerks and stenographers.

The sales manager is in charge of all sales activities. He formulates the sales policies and methods, supervises the salesmen, etc. The advertising department looks after all advertising matters, and it is not always under the jurisdiction of the sales department, although its activities are clearly related to selling. Many factories are not large enough to maintain an advertising department, but employ an advertising agency.

The shipping department is responsible for affixing the proper tax revenue stamps on all cigars leaving the factory as, under government regulations, the stamps are to be affixed just prior to shipment. The shipping clerk prepares bills of lading or other

suitable records for all shipments and turns them over, with his shipping order, to the invoice department for billing to customers.

Trade terms are usually 30 days net, with 2 per cent. cash ten days. In special cases the invoice dating may be advanced from a few days to a month or more, depending upon the nature of sale. All cigars are billed at list prices, less trade discount, which varies from one to twelve per cent. Special rebates, based on number of cigars purchased or their monetary value and calculated at various rates, are also given to customers who buy in large quantities. Retailers buying from jobbers may be granted a small rebate by the company. This rebate is allowed on purchase of a certain number of cigars containing certain brands. It is paid direct to the retailer by the company upon advice from the jobber.

The market for the company's product is generally confined to a restricted area, usually the state in which the company's factory is located and the surrounding states. Some factories, however, have a national market. The biggest part of the company's product is sold to jobbers; the balance, in order of volume, goes to chain stores dealing in tobacco products, large individual retailers and small local retailers through local salesmen.

The cost of distribution consists of the packing and shipping expenses, freight outward and the ordinary selling expenses. The largest item of selling expense generally is advertising in newspaper, magazine, billboard, window and counter displays, electric and other signs, etc. Inasmuch as it is often desirable to know whether a certain territory or a certain salesman is profitable, the sales and the relative distribution expenses are analyzed accordingly.

The financial records consist of the usual cash receipts and disbursements books, purchase or voucher register, sales register, journal, general ledger and subsidiary ledgers for accounts receivable, accounts payable, stock and factory costs. Comment on the books of original entry and the receivable and payable ledgers is unnecessary. The stock ledgers and their use have been described.

The general ledger is divided into sections, one each for accounts relative to the following classifications, assets, liabilities, capital, revenue, cost of sales, selling expenses, administrative expenses and sundry expenses. Control over the factory cost ledger is maintained by the goods-in-process account, to which are charged

the materials and supplies, as requisitioned, all labor and factory burden. This account is credited with the finished goods at cost, as determined by the cost sheets.

Amounts charged to goods in process in the general ledger are distributed in the factory ledger to appropriate detail accounts. These accounts are not closed into total or process costs during the year; consequently it is not necessary to enter credits for finished product. The factory ledger is only an analysis of operation costs, agreeing in its periodical totals with the charges to the controlling account. After each period's details have been compared with the control, cumulative totals are brought down for the purpose of such reports on the operations of the year to date as may be desired. These totals are a valuable aid in setting up a budget of operations for the succeeding year and in preparing the income-tax returns for the current year. The factory ledger is supported by adequate production and cost sheets, covering each brand of cigar and corresponding in total to the cost details.

The balance-sheet and profit-and-loss account may be prepared as follows:

BALANCE-SHEET

Assets

Current assets:

Cash in bank and on hand.....	xxxxx	
Marketable securities.....	xxxxx	
Notes and accounts receivable:		
Customers' notes receivable.....	xxxxx	
Customers' accounts receivable.....	xxxxx	
Miscellaneous.....	xxxx	
	=====	
	xxxxx	
Less reserve for bad debts.....	xxxx	xxxxx
	=====	

Inventories—priced at cost:

Cigars.....	xxxxx	
Material:		
At factories and warehouse.....	xxxxx	
With vendors.....	xxxxx	
In bond.....	xxxxx	
Total materials.....	xxxxx	
Supplies and revenue stamps.....	xxxxx	xxxxx
	=====	=====

Prepaid expenses:

Advertising supplies.....	xxxx
Insurance.....	xxxx

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Taxes.....	xxxx	
Stationery and supplies.....	xxxx	xxxx
Advances to officers and employees.....		xxxx
Investments at cost.....		xxxxx
Property, plant and equipment:		
Land.....	xxxxx	
Buildings.....	xxxxx	
Machinery and equipment.....	xxxxx	
Furniture and fixtures.....	xxxxx	
Automobiles and trucks.....	xxxxx	
	xxxxx	
Less reserve for depreciation.....	xxxxx	xxxxx
Cigar machinery leased—charges under contracts, less provision for amortization.....		xxxxx
Goodwill and trademarks.....		xxxxx
Total.....		xxxxx

Liabilities

Current liabilities:		
Notes payable.....	xxxxx	
Accounts payable—trade creditors'.....	xxxxx	
Accrued expenses.....	xxxxx	
Provision for federal income tax.....	xxxxx	
Dividends payable.....	xxxxx	
Total current liabilities.....		xxxxx
Bonds or mortgages payable.....		xxxxx
Capital stock:		
Authorized and issued:		
Preferred xx cumulative—xxxx shares of xx each.....	xxxxx	
Common—xxxx shares of xx each.....	xxxxx	xxxxx
Surplus.....		xxxxx
Contingent liabilities.....		
		xxxxx

PROFIT-AND-LOSS ACCOUNT

Gross sales.....		xxxxx
Less:		
Return sales.....	xxxx	
Freight.....	xxxx	
Discounts and special rebates on sales.....	xxxx	xxxx
Net sales.....		xxxxx

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Cost of sales:		
Purchases of tobacco and supplies—less discounts	xxxxx	
Direct labor	xxxxx	
Revenue stamps	xxxxx	
Manufacturing expenses	xxxxx	
		xxxxx
Less:		
Increase in inventory	xxxxx	
Sales of stems and cuttings	xxxxx	
Free cigars	xxxxx	xxxxx
		xxxxx
Cost of sales		xxxxx
Gross profit		xxxxx
Expenses:		
Shipping and delivery	xxxxx	
Selling expense	xxxxx	
Advertising	xxxxx	
Administrative and general	xxxxx	
		xxxxx
Total expenses		xxxxx
Net operating profit		xxxxx
Miscellaneous income:		
Dividends received	xxxxx	
Interest received	xxxxx	
Sundry	xxxxx	
		xxxxx
Less miscellaneous charges:		
Interest paid	xxxxx	
Sundry	xxxxx	xxxxx
		xxxxx
Miscellaneous income—net		xxxxx
Net income before income tax		xxxxx
Provision for income tax		xxxxx
Net income		xxxxx

In the main, the balance-sheet and the profit-and-loss account of the cigar manufacturer follow those of other manufacturing establishments. Special attention, however, must be given to certain matters in each of the statements.

Balance-sheet. Most cigar manufacturers value their inventories at actual cost, regardless of market value. Under federal income-tax laws the inventory may be valued at average cost if desired. The basis of valuation must be indicated. Raw material is segre-

gated according to location, to show (1) what is immediately available and (2) that upon which a further cost may have to be added when delivered. Material in vendors' possession will be subject to freight charges and that in bond to duty. The leased cigar machinery should not be included in the property accounts. The investment in them is a deferred expense.

Profit-and-loss account. Gross sales are shown after regular list discounts have been deducted. Cash discounts and special rebates on sales are shown separately. Payment for revenue stamps should not be included in the purchases, as this is not a cost of material. Sales of stems and cuttings (the proceeds of which are relatively small compared with actual cost) are deducted from cost of sales as these things are not sold to the cigar trade. Advertising expense is shown separately and usually is of considerable amount. Manufacturing, shipping and delivery, selling, administrative and general expenses should be shown in detail in a supporting schedule.

Audit of a cigar-manufacturing company does not differ to great extent from that of any other manufacturing enterprise. The auditor should satisfy himself that all income is properly accounted for and that proper distinction is observed between charges to capital and to expense accounts. Royalties paid for the use of leased machines should be verified by the cigar-production records.

Classification of factory payrolls and overhead should be examined as to propriety. The issuing and accounting for materials, especially tobacco, should be subjected to close scrutiny, for, if there be carelessness in handling, it will have a bearing on the gathering of accurate cost information.

The inventory, which is usually the largest item on the balance-sheet, should receive careful consideration. It is the practice of some manufacturers to include, in their inventory, interest charges for the use of capital. All such charges should be eliminated. The methods of pricing for the opening and closing periods should be on one basis. The auditor should see that duty paid on imported tobacco in the inventory is included in its valuation and that no duty is included in the value of tobacco in bonded warehouse. Material in the hands of vendors or outside storage warehouses should be verified by correspondence. Work in process, which is generally of comparatively small amount, should be valued according to the varying stages of production. The valu-

ation of finished cigars should not include the value of revenue stamps, unless the stamps have actually been attached. Packages to which the revenue stamps have been affixed should be few in number, as, under government regulations, the stamps are not to be affixed until the cigars are about to be shipped.

Shortly after January 1st of each year, government auditors make an examination of the records of consumption, stock on hand, etc., to satisfy themselves of the correctness of the inventory and to determine if the proper amount of tax has been paid. In making an audit after such examination, the government's examiners' report may be used as positive proof of tax liability. If no official examination has been made, the auditor should satisfy himself that all requirements have been met.