Capital Surplus

By R. R. Thompson

The Canadian companies act, 1934, makes several references to capital surplus, but nowhere does it attempt to define it. The result has been, on the part of many, much studying of the authorities, who, unfortunately, are almost as bad, and only make occasional attempts to define capital surplus, while they refer to it many times. Generally they content themselves with saying in different places that such and such a thing is or is not to be regarded as capital surplus. It is the purpose of this article to examine the definitions that we have, to consider the various things which are regarded as capital surplus, and to attempt to draw therefrom a definition wide enough to embrace the best ideas and yet strict enough to keep us on sound ground, and so to avoid the wideness of the marsh.

Let us first clearly understand what we are and are not discussing. As Kester writes, the term "surplus" in its broadest sense represents the

"difference between the net worth of the business and the capital stock issues outstanding, i.e., the sums credited to the various capital stock accounts."

Most writers agree that when the words "revenue" or "capital" are used to govern the word "surplus," they indicate the origin of that surplus. Surplus may result from profits earned or made, or it may result from contributions or gifts. Hatfield in referring to the two different systems of classifying portions of the surplus, writes:

"According to one they are given descriptive titles which relate to the purpose of their establishment; according to the other they are labeled in accordance with the source whence they were derived. Thus the sinking-fund reserve and reserve for extensions relate to the purpose, while donated surplus and capital surplus refer to the source."

Here, in the use of the word "source" he is referring to the transaction. All profits must rise from the capital somehow, but distinction must be made between surplus that arises out of a capital as distinct from a revenue transaction.

Now, we are not dealing with revenue surplus, which results from the accumulation of revenue profits. I believe that the following definition of revenue profits combines and coördinates the opinions of the most conservative authorities:

"The net revenue profit or income of a business for a period is the surplus remaining from the earnings resulting from the regular operations of the business after providing for all known, paid and accrued, and probable costs, expenses and wastages, resulting from the regular operations of the business during that period. It will also include revenue by way of dividends or interest from investments outside the business."

When made, revenue profits can only be realized profits. By "realized profits" I mean profits which are represented by cash or an obligation to pay cash at the present or a future date, or as Pixley puts it "profits tangible for the purpose of division." Profits may have been realized at one time but later may have become invested in fixed assets. In that case they are certainly not available for distribution, except by way of stock-dividends. Some writers contend, with Finney, that "there is no profit without realization," and all agree that unrealized profits must never in any circumstances be used as supposed justification for the payment of a cash dividend.

We are not dealing with capitalized surplus, which, as its name indicates, is surplus which has been capitalized. One could define it as follows:

"Capitalized surplus is surplus, no matter whether it resulted from capital or revenue transactions or from contributions, which has been appropriated, so that it forms part of the permanent capital investment of the concern and accordingly can not be distributed by means of cash dividends or used for the purpose of writing off losses, except on a reduction of capital, as provided for under the company law concerned."

The most common method of capitalizing surplus is by the payment of a stock-dividend. Also, it is evidently the intention of section 61 of the companies act to provide for the capitalization of surplus used for the redemption or purchase for cancellation of preferred shares.

I think that those who wrote section 61 intend something, but that they only state part of their intention. Where preferred shares are redeemed by means of an appropriation of surplus, and such redemption results in a profit, there are two items of surplus concerned:—

(a) The net profits or surplus, which are represented by liquid assets available and are used for the redemption, and

(b) The excess of the par value of the preferred shares over the figure at which they were redeemed.

That is to say, if $100 preferred shares are repurchased at $90, then (a) = the $90 paid in cash, and (b) = the $10 capital profit.

The fifth line from the end of sec. 61 contains the following words:

"the surplus *resulting from such redemption* or purchase shall be designated as a capital surplus, which shall not be reduced or distributed by the company except as provided in sections forty-nine to fifty-eight, both inclusive, of the act."

The words in italics indicate (b) only. The surplus appropriated (a) was in existence already. Yet (a) the surplus appropriated for the redemption will replace the preferred stock redeemed in the balance-sheet, and to my mind should be regarded as capitalized, no matter whether such surplus originally arose out of capital or revenue transactions. It is probable that this is what they intended in the act, although they have not said so. I suggest the amendment of the last five lines of sec. 61, by the insertion of the words italicized in the following:

"And *any* surplus resulting from such redemption or purchase for cancellation *at less than the par value of the shares together with the ascertained net profits of the company which had been set aside by the directors for the purposes of such redemption or of such purchase for cancellation,* shall be designated as *capitalized* surplus, which shall not be reduced or distributed by the company except as provided in sections forty-nine to fifty-eight, both inclusive, of this act."

I think that sound accounting and finance require this to be done. The account to be credited could be entitled, "Preferred shares redemption surplus: capitalized." This item should be grouped with the common and preferred stock capital.

As to the principal subject of discussion, capital surplus, may I quote from various authorities? Among the writers from Britain, Dicksee refers to "profits on account of capital," and elsewhere in reference to profits which do not arise out of the business of a company, writes:

"Leaving upon one side the most usual source of profit of this description—viz, the sale of a portion of the company's undertakings . . . the most ordinary classes of profits to come under this heading would be premiums received on shares or debentures, or cash which has been paid up upon shares forfeited."

NOTE.—Premiums on redeemable bonds and debentures are revenue items, being the exact counter-part of discount, which is really interest paid in advance. The practice now is to amortize the premium or the discount over the life of the bonds or debentures.

Dickinson writes:

"In setting forth the results it is imperative that extraordinary profits or losses not arising out of operations nor in the ordinary course of business, such, for instance, as those resulting from sales of portions of capital assets, should be either eliminated or stated separately."

Spicer and Pegler refer to "losses on capital assets occasioned by the abandonment of assets." They also discuss "the question as to whether capital profits are available for the payment of dividends" and refer to several cases. In *Lubbock* v. *The British Bank of South America* a profit of £205,000 had been made on the sale of a part of the undertaking of the company. It was held that:

"the £205,000 was plainly profit on capital . . . for that sum was the surplus ascertained after the liabilities and capital were placed on one side of the account and the assets on the other. Under the articles of the company the directors were justified in carrying over the £205,000 to a profit-and-loss";

and distributing it by way of cash dividend, if permitted by the articles of association or by-laws of the company.

In *Foster* v. *The New Trinidad Lake Asphalte Coy. Ltd.*, it was a case of the realized appreciation of an asset. The asset, a book debt, would ordinarily be regarded as a current asset, but in this case it had been taken over by the company from another concern, together with other assets, when the New Trinidad company was formed. Accordingly, this book debt did not come on the books of the company as a result of its ordinary business, but as a result of a capital transaction. The purchase consideration for these assets was a portion of the capital-contributions of the New Trinidad company: these assets formed part of the capital investment of the company. This book debt, when taken over, was regarded as worthless, but subsequently it was collected in full, with interest accrued, realizing £26,258—16/—. The court held that this was a "realized accretion to the estimated value of one item of the capital assets." It was held that this profit was available for dividend, if the company's articles or by-laws permitted and if there had been a revaluation of the whole of the assets of the company and such surplus was not required to make good losses on other assets. Spicer and Pegler also point out that:

"capital profit arising on a bona-fide revaluation of fixed assets can be utilized to write off a debit balance on the profit-and-loss account arising in prior periods, thus enabling dividends to be paid out of current profits. (*Ammonia Soda Co.* v. *Chamberlain*)."

Smails, when dealing with the dividend fund of a limited company, writes as follows regarding capital profits and losses:

"A capital profit for purposes of this discussion is a profit resulting from dealing in fixed assets. Mere appreciation in market value of fixed assets which are not for disposal does not give rise to any profit, and if brought on to the books should be credited to surplus resulting from appraisal of fixed assets. A true capital profit can be said to result from the sale of a portion of the fixed assets at a price in excess of their net book valuation when the fixed assets remaining unsold are carried at figures not exceeding their realizable values. But the difficulty of ascertaining the realizable values of such assets as land, buildings, plant, etc., renders it inadvisable to regard the gain on disposal of an isolated portion of such assets as a profit. Rather, it should be credited to some form of non-distributable reserve. . . .

"A capital loss is either the converse of the profit discussed above, or is the result of the destruction of a fixed asset by accident or act of nature. Such a loss constitutes an impairment of capital."

Ferguson and Crocombe write as follows:

"A revenue surplus or earned surplus is built up by withholding from distribution a portion of the net profits derived from ordinary operation. Capital surplus does not have its source in operations. If shares are issued at a premium, the legal or stated capital is the par value and any excess of capital contribution above that amount constitutes a capital surplus.

"If a trading or industrial concern sells a fixed asset at a profit, this profit is not derived from the ordinary operations, but from the disposal of a fixed or capital asset, and may be properly termed a capital surplus. As will be brought out later when discussing shares without par value, the law in many cases permits a division of the amount obtained and only part thereof is set up in the accounts as a credit to capital stock, the balance of the amount received thus being separated and constituting a capital surplus. All amounts that constitute a capital surplus should be excluded from the operating accounts, and would be better shown under their own titles and on the balance sheet would appear as capital surplus. There is no income tax on such amounts, since income tax is based on operating earnings, not on accretions to capital."

Behind all of this we can see the idea of a surplus which arises out of a capital transaction, and not out of a revenue transaction —that is to say, not out of one which will arise regularly in the ordinary course of carrying on the company's business.

Let us turn to the writings of American authorities. Here we find more definition. Finney in the 1927 edition of his *Principles of Accounting* divides the surplus of a corporation into two main sub-divisions. One is "surplus earned through operations," by which he intends revenue profits as defined above. The other is:

"Surplus arising from other sources, which may be further subdivided as:

"(a) Paid-in or contributed surplus, arising from premiums on stock, and donations from stockholders in the form of stock or assets.

"(b) Surplus arising from extraneous transactions, such as sales of fixed assets.

"All surplus arising from other than operating sources may be credited to a single account called capital surplus; or separate accounts may be carried with the various items, such as premium on stock, donated surplus, special surplus from the sale of fixed assets, etc. But mere book entries writing up assets should not be credited to either surplus or capital surplus."

In another place he writes,

"profits on sales of buildings, equipment and securities owned are extraneous profits, unless the business regularly deals in these commodities."

He goes on to point out that losses on such transactions are extraneous losses. In his 1934 edition he divides the surplus into three sub-divisions:

(a) Operating profits;
(b) Paid-in surplus from premiums or from excess of paid-in over stated value of no-par stock, donations by stockholders or outsiders, profits from sale of fixed assets or donated stock;
(c) Unrealized accretions in market values of assets.

He points out that some accountants will describe (b) and (c) as capital surplus and that others will restrict the term "capital surplus" to (b), describing (c) as "reserves for unrealized profits"; and again that some will describe (a) and (b) simply as "surplus," describing (c) as "capital surplus." Because of this confusion he retreats a little from his former position, recommending that items should be credited to separate accounts, not to "capital surplus" account. This last recommendation may be wise, but it does not help accountants, who have to group items under the heading "capital surplus" for the Canadian companies act. It is interesting to note how the majority regard (b) as "capital surplus," and I think that the majority of Canadian accountants will prefer that unrealized accretions be credited to "reserve for unrealized profits," even though they can be regarded as a form of capital surplus.

The following quotations are taken from Hatfield:

"The account credited is given the descriptive title Surplus from Donated Stock. This is incontrovertibly correct, although it may be that a less cumbersome term would serve in its place, such as Capital Surplus. . . . A Surplus is truly converted when the donation is received by the corporation and is not dependent upon a subsequent sale." [This is an unrealized surplus]. "Premiums received upon stocks of railroads is, according to the rules of the interstate commerce commission, not to be credited to income": [therefore it belongs to capital surplus.] "Since premium on capital stock can not be classed as a profit 'arising from the business' it could not be paid as a dividend in states with this limitation": [Here he refers to the fact that in a number of states dividends are limited by statute to 'profits arising from the business.' When writing of profits earned through the ordinary course of the business he excludes from them] "at times such unusual gains as may have arisen through the sale of capital assets." [He refers again to unrealized surplus not arising from the ordinary course of the business in the following]: "The accumulation of surplus may also come through a recognition of the appreciation of capital assets even where there has been no sale. If this is shown at all, accountants generally agree that it should not appear among the current profits but must be put in some surplus account, perhaps with a distinctive title indicating its peculiar source."

Montgomery writes:

"Accretions to capital arising from reappraisals, from sales of capital assets, from gifts, from premiums on capital stock, etc., are known as capital surplus. . . . The excess of the book value of assets over liabilities and capital stock at the time of incorporation is known as paid-in surplus. Subsequent contributions by stockholders, in cash or property, when additional capital stock is not issued, are also a part of paid-in surplus. . . . There is no real distinction between capital surplus and paid-in surplus."

After discussing the possibility that plant or property accounts may have been excessively depreciated, and that apparent profits may arise as a result when a sale takes place, he recommends that when the capital assets disposed of are to be replaced, profits on such a sale should be transferred to special surplus or to replacement accounts and not be made available for cash dividends. Clearly, to me, excessive depreciation is an over-charge against revenue, and if indubitably discovered can properly be re-credited to revenue or earned surplus, but even so, as a rule, unless the amount at stake is negligible, it will be wiser to credit it to some replacement reserve. Montgomery concludes:

"It may be said, therefore, that profits arising from sales of capital assets are capital or special surplus or earned surplus, depending on the disposition of the proceeds."

Kester, in dealing with the classification of surplus as to source, writes:

"Among the more common sources of capital surplus may be mentioned:

"1. Capital stock premiums arising from the sale of par value stock for more than par, no-par value stock for more than stated value, and resale of treasury stock for more than its purchase price.
"2. Stock and other donations.
"3. Stock assessments.
"4. Purchase of own stocks below par or stated value.
"5. Conversion of one kind of stock for a lesser amount of another kind.
"6. In some states, forfeiture of stock subscriptions.
"7. Writing up of value of capital assets.

"As the above items constitute the more usual credits to surplus, so transactions which are the opposite of items 1, 4, 5 and 7 constitute the more usual debits to capital surplus. Other charges sometimes made directly to capital surplus (usually and better to earned surplus, however) are the extraordinary losses, such as fire loss."

Later he writes:

"Donations of cash or other property by the shareholders or gifts from the outside, such as factory sites and other bonuses, sometimes given to induce enterprises to locate in certain places, constitute sources of capital surplus."

He further states that:

"Capital surplus is of three kinds, according to its three chief sources, viz., paid-in, donated and re-appraisal. . . . In the operation of the business, capital surplus should ordinarily be limited to the same uses as capital stock. . . . basically it is contributed capital and will therefore be permanent. It should not be used for dividends, for such use was not contemplated when it was contributed."

It will be noted that Kester restricts the use of the term considerably, excluding profits from the sale of fixed assets; but later he writes:

"Earned surplus arising from capital profits—i.e., from the sale of capital assets—is also an ideal surplus for such use," (writing off re-appraisal losses).

Here he includes profit on the sale of a fixed asset as a capital profit. He also uses the term "earned surplus," to mean surplus arising from realized profits. In another place he writes that the title "surplus—i.e., earned surplus should be used to denote profits available for dividends."

I respectfully submit that it is wrong to use the word "earned" to designate profits which are realized or "tangible for the purposes of division" (Pixley), as distinct from those which are not realized. The Canadian companies act requires us to show earned surplus distinct from capital surplus, and accordingly we must get at the exact meaning of the word "earned."

The word "earn" comes from a group of old Teutonic words, which mean labor itself, work in the fields for the harvest, the reaping of the harvest and the harvest itself. In all cases it deals with labor and operations, which result or ought to result in a reward. Meanings given by various standard dictionaries (British and American) are as follows:

> To gain (especially money, wages, etc.) by work: to gain by labor or service: to obtain or deserve as the reward of labor: to gain by merit (to earn fame): to get as one's deserts or due (to earn a reputation for honesty): to gain as a due return or profit (money well invested earns a good return: money hired out is worked by others who pay interest for its hire).

In every case there is the idea of work of some kind, physical or mental, which obtains, or at least deserves, a reward—it earns a reward. We can see, therefore, that it is quite wrong to use the word to designate profits or rewards which can be divided; because frequently a laborer will earn a reward, which he does not receive, simply because for some reason it is not available for distribution, or, as the majority of writers would put it, it is not in a realized form. The word has to do with laboring operations or work of some kind, which gains or ought to gain a reward. Nowadays the work is done not only by men, but also by machinery and other assets. I submit that the phrase "earned profits" should never be applied to gifts or those profits of an unusual nature which do not result from the regular operations, but from windfalls and other fortunate occurrences which may never occur again. It will be found that practically all of these unusual profits result from transactions in capital assets, capital liabilities, capital stock or substantially the entire assets of an undertaking. The word "earned" must always be associated with labor of some kind; it would be unwise for any of us to attempt to give it a meaning differing from that accepted by the standard dictionaries, to say nothing of many standard writers in accounting. I believe that the phrase "earned surplus" refers to any accumulation of balances of net operating profits. As Montgomery writes:

"Earned surplus should represent net income derived from the normal operations of a business."

Again, it would be wise to follow the majority of standard writers in the use of the phrase "capital profit" and, to regard the word "capital" as indicating the nature of the transaction that gave rise to the profit. Accordingly, capital profits will form the capital surplus. Kester's broad definition of surplus was given at the commencement of this article.

Accounting terminology, published by the American Institute of Accountants, contains the following definition:

"Surplus, capital: Capital surplus comprises paid-in surplus, donated surplus and revaluation surplus—that is, surplus other then earned surplus; surplus not arising from profits of operation but from such sources as sale of capital stock at a premium, profit on dealings in a corporation's own stock, donated stock, appraisal valuation and surplus shown by the accounts at organization."

It will be noted that profit resulting from the sale of a fixed or capital asset is not included. The report of a special committee on the definition of earned surplus, which was presented at the annual meeting of the American Institute of Accountants in 1930 was not adopted. One of the definitions given in this report included "profits from the disposition of any corporate asset" as earned surplus. Because of this evident disagreement we must turn elsewhere. Capital surplus certainly includes the items given in the definition above; but most authorities agree that it can also include profit from the sale of a fixed or capital asset. Saliers in *Accountants' Handbook* takes the broad view as the following statement shows:

"Surplus in its common use, consists of the accumulated undivided profits of the business. Sometimes, however, it is derived from sale of stock above par, from sale of capital assets or from a revaluation of assets, in which case it is capital surplus."

"Capital surplus comprises all surplus not derived from ordinary operations and is classified as:

"1. Unusual or extraneous profits.
"2. Premium on sale of capital stock.
"3. Forfeited payments on stock subscriptions.
"4. Assessments on fully-paid stock.
"5. Amount by which redemption price of stock retired is less than par.
"6. Excess of value of tangible property over stock for which it is received in payment.
"7. Profit on sale of treasury stock repurchased for value. Items 2–7 constitute paid-in surplus."

Again he states that:

"Capital surplus may arise from any of the following causes:
"1. Sale of capital stock at a premium,
"2. Gifts,
"3. Sales of capital assets at a profit,
"4. Increases in asset values through appraisals,
"5. Capital contributed by stockholders without issuance of additional stock.
"6. An excess of assets over liabilities and capital stock at time of incorporation of company.

"The two last-named items are usually called paid-in surplus."

Finally, when dealing with the sale of capital assets he writes:

"Credit excess of sale price of capital assets over their depreciated value to a special reserve account or to capital surplus, rather than consider such amount as earnings. However, where the difference is relatively small it is generally carried to earned surplus."

With the last sentence few are apt to quarrel, because there he has in mind small items, which are too small to be of any importance one way or the other and might cause troublesome apportionments and estimates to find out if there had been excessive depreciation.

There is a consensus of opinion in favor of capital surplus as broadly defined by Saliers. Some would regard profit on the sale of fixed assets as a profit from operations, but the majority would regard it as an unusual profit, one from a capital transaction, and accordingly as contributing to "capital surplus." Others again prefer not to countenance "unrealized capital profits," and yet, cautious as one must be in dealing with such profits, they undoubtedly occur: all agree that such profits should be credited to some reserve, named clearly to show its origin. Others make a distinction between profits and contributions, but they all contribute to surplus, and there is no essential difference between a profit resulting from the sale of a fixed asset and a gift of a land-site. However, under the Canadian companies act so-called "distributable surplus" must be shown separately, although in essence it is a capital surplus.

I would make the following suggestions:

(a) The word "realized" should be applied only to profits, when they have once been represented by cash or by an obligation to pay cash at the present or a future date.

(b) The word "earned" should be used only for profits from the regular operations of the business, or from money invested outside the business, using the definition given at the commencement of this article for net revenue profits: in other words "earned profits" and "revenue profits" will have the same meaning.

(c) The term "distributable-surplus" should be replaced by "contributed or paid-in surplus," because both earned and capital surplus are distributable in proper circumstances.

(d) Capital surplus is built up by profits and contributions arising from capital transactions or happenings—that is to say transactions in the capital assets, capital liabilities, capital stock or funds of a concern—or a transaction concerning the sale or purchase of substantially an entire undertaking. Accordingly, it may arise from the following:

(a) Profit on the sale, acquisition, revaluation of a capital or fixed asset.

(b) Profit on the sale or acquisition of current assets in the sale or acquisition of substantially the entire assets of an undertaking.

(c) Profit on the redemption of a capital liability at less than its "present net worth" to the borrower.
(d) Profit on a transaction concerning the capital stock of a company.
(e) A gift or payment of funds for capital purposes.

The following may be helpful:

Realized profits and contributions.

(a) Sale of a factory building at more than its net depreciated book value, assuming that full or proper depreciation has been written off in the past.
(b) Purchase of a business including outstanding book-debts or stocks of goods on hand, some of which are regarded as of little or no value: a capital profit arises if these latter are realized at a figure in excess of their purchase price.
(c) Purchase by a company of its own bonds. For example:

Capital liability on bonds (issued at discount)...		$100,000
Discount unamortized as per last balance-sheet.	$3,000	
Less		
Discount to be amortized out of revenue to date of purchase......................	200	
Discount unamortized at date of purchase.....		2,800
Present value of bond.......................		$97,200
Cash purchase-price of bond.................		96,000
Capital profit...........................		1,200

(d) (i) Redemption by purchase of a company's own preferred stock at a price (say market) which, at the time, is less than the par value of the stock.
(ii) Premiums on the issue of common or preferred shares. So-called "distributable-surplus" is of the nature of such a premium, although it must be stated as a distinct item in the statement of surplus.
(iii) Additional payments by stock or bond holders of one class for the privilege of changing their holdings into another class.
(iv) Forfeiture of stock. In this case the profit equals the amount paid up on the shares, but it is not properly realized until the shares have been re-issued, because this may be at less than par, so that a portion of the profit will be sacrificed. Until the shares declared forfeited are re-issued the

profit should be credited to "forfeited shares suspense." After the shares are re-issued and the profit is finally realized it should be credited to "profit on forfeited shares."

(e) A pro-rata assessment agreed to by one or more classes of shareholders for the purposes of making good a loss of capital.

Unrealized profits and contributions

(a) (i) Donation of a capital asset, such as a factory site, by a municipality. It is assumed that any extra expenditure, incurred in complying with the conditions laid down before the transfer of the property can take place, will have been debited as part of the cost of acquisition and accordingly will have reduced the profit. The profit will be the excess of appraisal value over such costs.

(ii) Purchase of the shares of a subsidiary company at a price less than their true value.

(iii) Discovery of a hitherto unknown mineral deposit, enhancing the value of land.

(iv) Appreciation from the re-valuation of an asset.

(b) Donation of a company's own shares to trustees to be disposed of for the benefit of the company. When the shares are sold the adjusted profit becomes a realized profit.

Losses of capital can result from revenue operations, capital transactions or in other ways; but capital losses as distinct from revenue losses result from capital transactions or happenings. If the word "loss" be substituted for the word "profit" they can arise out of (a) or (b). In the case of (a) destruction of current assets in some disaster, such as a fire or an earthquake, could be regarded as a capital loss. The following are examples:

Realized

(a) (i) Loss on sale of fixed assets.

(ii) Loss of assets by fire not covered by insurance.

(iii) Loss of assets due to some convulsion of nature, such as an earthquake.

(b) Loss on sale of substantially the entire undertaking.

Unrealized

(a) Loss on re-valuation of fixed assets, where proper depreciation has been provided for, as in the case of abandoned plants, or machinery and equipment installed for a special purpose which has not proved successful.

Whatever may be the difficulties of differentiation between earned and capital surplus, we can not question the Canadian government's action in ordering them to be stated separately. There are many legal decisions which make the distinction and show that it is necessary. It is not always essential to make good capital losses before paying dividends out of revenue profits, although, as a rule, not to follow such a policy is highly unwise; but there is no question that capital profits must be used first in making good capital losses. After that, unrealized capital profits should be transferred to specially named reserves, although, if the profit has resulted from the acquisition of a fixed asset, such as a land-site, it may be used for a stock-dividend, but, of course, never as supposed justification for a cash dividend. As to realized capital profits, which are not required to make good losses or to build up reserves, if the company's finances and its own charter and by-laws permit, they may be distributed by way of cash dividend.

In conclusion, may I hope that out of the discussion now in progress, accountants of the English-speaking world will come to definite conclusions as to what these important terms really mean, and are going to mean to all of us. For this purpose I suggest that we keep strictly to the established meaning of words. We speak a common language, the words have established meanings, and accounting terms also should have common meanings for all of us, which should be in harmony with our common tongue.

Quotations in this article have been made from the following, to all of whom I express indebtedness: Committee on terminology, American Institute of Accountants: *Accounting Terminology.* L. R. Dicksee: *Auditing.* Sir Arthur Lowes Dickinson: *Accounting, Practice & Procedure.* H. A. Finney: *Principles of Accounting.* H. R. Hatfield: *Accounting, Its Principles & Problems.* R. B. Kester: *Advanced Accounting (vol. 2).* R. H. Montgomery: *Auditing, Theory & Practice.* F. W. Pixley: *Duties of Auditors.* E. A. Saliers: *Accountants' Handbook.* R. G. H. Smails: *Auditing.* Spicer & Pegler: *Bookkeeping & Accounts; Practical Auditing.* W. S. Ferguson and F. R. Crocombe: *Limited Companies and their Accounts.*