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Such is the general structure of the income statement. All income statements are based on the principles embodied therein, whether they be more highly refined and elaborate, or more simple and condensed. For the period which it covers an income statement represents a tug-of-war, as it were, affecting the capital invested in the business. Sales forces are at work trying to increase the capital by selling goods at higher prices. Buying forces are endeavoring to purchase the goods at the lowest possible prices. The administrative division is constantly striving to keep expenses at the minimum point consistent with efficiency. Directors undertake the task of borrowing capital as cheaply, and employing it as economically, as possible.

How well these various forces of organization have succeeded in their efforts is shown by the income statement. This question may be judged by studying percentage relationships, by comparing the data of one period with those of prior periods, with the data of similar companies, and with the average of groups of similar companies. Ability to interpret the causes of fluctuations also is useful in this respect. Another valuable test is the percentage of return on invested capital, as is also the number of times the capital has been turned over.

The income statement is a fertile source of information. It is not strange that it has been characterized as representing the dynamic forces of business enterprise. Somewhat like electricity, the results are apparent, but the way in which these forces accomplish the results is something of a mystery.

A thorough study and understanding of the functions of the income statement and the relation to the balance sheet, not merely as a balancing statement for tying up the surplus, would add greatly to the accountant's equipment in his attempt to interpret the operations of a business, and make the resulting information useful to clients.

Acceptances Under Letters of Credit Against Merchandise Received Under Trust Receipt

(*Reprinted from the July*, 1930, *Bulletin of the American Institute of Accountants*)

ONE detail in accounting practice concerning which there seems to be some lack of knowledge, or lack of consideration on the part of accountants, is the treatment of acceptances under letters of credit. In order to avoid misunderstandings it is important that accountants should be thoroughly informed regarding the handling of such transactions.

Ordinarily banks issuing letters of credit either hold documents evidencing possession of the merchandise against which they have accepted drafts, or have delivered the merchandise to the customer on a trust receipt. In either case, the bank holds title to the merchandise, as the trust receipt states that the merchant or manufacturer holds the merchandise at all times in trust for the bank, or if sold, the accounts receivable or proceeds of the sale, as security for the payment of the draft. A bank rarely delivers merchandise under acceptances without securing a trust receipt.

Often it would be difficult to identify or segregate the pledged assets, because the merchandise released to the manufacturer on trust receipt may have gone into manufacture and lost its identity before the liability has been discharged. In such cases it is impossible for the accountant to show the specific asset pledged, but it is important to indicate that the bank, theoretically at least, has recourse to the merchandise ahead of any other creditor should the acceptance not be paid. Proper accounting requires that all secured liabilities should be captioned as such.

Acceptances under letters of credit may be described in various ways, but a de-

scription which seems to cover this adequately is the following: "Acceptances under letters of credit against merchandise received under trust receipt." This is an exact statement of fact. It is not asserted that the item is collateraled by anything or secured by anything, because neither statement might be correct in the sense that would apply to a regular collateral loan. Everybody, though, who understands the nature of a trust receipt is put on notice that the holder of these acceptances has a lien on certain of the assets which comes ahead of other creditors.

Banks are sometimes blamed for not reporting to the accountant the fact that they hold a lien on the assets covered by acceptances. In some instances the bank may be careless, but at other times the fault lies with the accountant. Frequently the forms used by accountants in confirming liabilities with banks do not call for information covering acceptance credits. Banks have to be careful in reporting dealings with customers and usually feel that they should not volunteer details not called for on the confirmation blank. Accountants should familiarize themselves with the handling of acceptance credits and should frame their questions to the banks with sufficient completeness to cover all important phases of these transactions. If acceptances are known to exist, the accountant should satisfy himself that he has all the facts and should present them properly.

Michigan Corporation Law

THE present Michigan law governing corporations, as amended under Act 267 of the 1929 law, now contains certain provisions which are likely to cause difficulty of interpretation and application when questions affecting surplus and dividends arise.

The law now attempts to define surplus in the following terms:

"The excess, if any, at any given time, of the total net assets of the corporation over the amount so determined to be capital shall be surplus available for all purposes for which surplus earnings may properly be applied."

From this, surplus earnings usually being subject to appropriation for dividends, one may reason that any excess of net assets over stated capital may be appropriated for dividends. If this conclusion is correct, any surplus, regardless of how derived, may be so treated. This would apply to capital surplus of any kind, not omitting that so-called capital surplus which sometimes is said to result from appraisals.

In further respects the present law has been changed to permit of greater latitude in the treatment of capital. Boards of directors now may determine, as in Delaware corporations, that only a part of the consideration received for capital stock shall be capital. But, as in Ohio corporations, the determination must be made at the time of issuance, if cash is the consideration, or within sixty days after the issuance, if the consideration is property, or partly cash and partly property. The limitation of time imposed upon corporations which had issued capital stock prior to the date on which the amendment became effective, was fixed at July 1, 1930.

Out of the new law one may read such provisions as that capital stock without par value may not be issued except for some consideration. The consideration may be that which is prescribed in the articles of incorporation, or the fair market value as fixed by the directors, whose judgment in the absence of fraud is conclusive, or such consideration as shall be consented to by two-thirds of the shareholders of each class of stock outstanding.

Again, one discovers that premium on shares having a par value may be treated as surplus available for dividends. This is by reason of the passage which reads: " * * * unless all the shares issued shall