[Journal of Accountancy](https://egrove.olemiss.edu/jofa?utm_source=egrove.olemiss.edu%2Fjofa%2Fvol44%2Fiss6%2F1)

Volume 44 | Issue 6 Article 1

12-1927

American Institute of Accountants Examinations, November 17 and 18, 1927.

American Institute of Accountants. Board of Examiners

The JOURNAL *of* ACCOUNTANCY

Official Organ of the AMERICAN INSTITUTE OF ACCOUNTANTS

Vol. 44 DECEMBER, 1927 No. 6

AMERICAN INSTITUTE OF ACCOUNTANTS EXAMINATIONS

[Following is the text of the examinations in auditing, law and accounting presented by the board of examiners of the American Institute of Accountants, November 17 and 18, 1927.]

Examination in Auditing

NOVEMBER 17, 1927, 9 A. M. TO 12:30 P. M.

The candidate must answer all the following questions:

No. 1 (8 points):

Name three ways in which a secret reserve may be created.

No. 2 (12 points):

The directors of the X company frankly admit the existence of secret reserves, justifying the practice on the ground that they are making provision for equalizing dividends in bad years, and ask you to certify to their statement and balance-sheet nevertheless. You have confidence in their good faith. What should you do?

No. 3 (10 points):

Comment upon each of the following certificates, limiting your remarks to 30 or 40 words on each one.

(1) We have audited the accounts of the A. B. Co. for the year ended December 31, 1926, and now certify that the above balance-sheet has been prepared from the books.

(2) We have audited the accounts of the A. B. Co. for the year ended December 31, 1926, and now certify that the above balance-sheet has been correctly prepared.

(3) We have prepared the above balance-sheet of the A. B. Co. at December 31, 1926.

(4) We certify that the above balance-sheet of the A. B. Co. at December 31, 1926, has been prepared from its books and is correct. We have not audited nor verified the accounts.

No. 4 (8 points):

Outline briefly your methods of procedure in the audit of one of the following industries:

(1) Motion-picture production.
(2) Aircraft construction.
(3) A company producing lumber from its own timber.

No. 5 (10 points):

In auditing the accounts of a trading company, you are unable to take or to supervise the actual inventory because of lack of technical knowledge as to values, and you are forced to accept a certificate of inventory from the responsible officers. Give an illustration of the form you would accept, and state what, if any, further steps you would take in verification of the values submitted.

No. 6 (12 points):

In making a detailed audit, how would you verify the cost of fixed property; i. e. land, buildings, plant and machinery?

No. 7 (10 points):

Define and give an example of each of the following terms:

(a) Depreciation
(b) Depletion
(c) Amortization
(d) Appreciation
(e) Contingent asset
(f) Contingent liability
(g) Deferred income
(h) Other income
(i) Special charges to profit and loss
(j) Appropriated surplus

No. 8 (10 points):

Where on the balance-sheet should the following reserves be shown? Give reasons briefly.

(a) Reserve for depreciation.
(b) Reserve for depletion.
(c) Reserve for bad debts.
(d) Reserve for federal taxes.
(e) Reserve for bond sinking fund.

No. 9 (10 points):

State the distinction between prepaid expenses and deferred charges, giving an example of each class. Explain why it is improper to combine them in one item on the balance-sheet.

No. 10 (10 points):

(a) Does the certificate of an accountant constitute a guaranty by him?

(b) What is the value and significance of his certificate? Discuss fully.

Examination in Accounting Theory and Practice

PART I

NOVEMBER 17, 1927, 1 P. M. TO 6 P. M.

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

No. 1 (48 points):

The Pacific Logging Company completed its first year of logging operations on December 31, 1926. A list of balances from the company's ledger (before closing) at December 31, 1926, was as follows:

Capital stock			$4,200,000
First mortgage 7% bonds			700,000
Timber		$4,000,600	
Booming ground		9,000	
Main railroad	$309,641		
Subsidiary railroad	235,000		
		544,641	
Logging engines, machinery and camp equipment		703,000	
Cash in bank and on hand		23,250	
Notes and accounts receivable		113,700	
Notes and accounts payable			40,737
Furniture and fixtures—city office		2,137	
Unexpired insurance premiums		4,134	
Reserve—depreciation			72,210
Wages accrued			23,780
Property taxes accrued			59,575
Labor and expenses:			
Felling and sawing	96,075		
Yarding and loading	102,460		
Scalers	8,837		
Rigging	33,273		
Hauling	135,040		
Booming and rafting	13,577		
		389,262	
Sales			974,500

Maintenance—railroads	$32,015		
" —camp	4,710		
		$36,725	
Depreciation—logging engines, machinery and camp equipment	$71,997		
Depreciation—city office furniture and fixtures	213		
		$72,210	
Insurance—industrial	13,403		
" —on equipment (fire)	8,075		
		21,478	
Property taxes		59,575	
Superintendence		11,970	
Administrative salaries		19,415	
Interest—on bonds	49,000		
" —on notes payable	1,647		
		50,647	
Fire-patrol expense		4,733	
City office expense		4,325	
		$6,070,802	$6,070,802

In arriving at the results of its operations for the year 1926, the company's officers had not considered depletion of timber cut for the year nor the amount which should be charged to cost of operations in respect of amortization of railway construction.

The trustees for the bondholders require a statement of profit and loss for the year 1926 showing the average cost of logs cut and of logs sold, also a balance-sheet as at December 31, 1926.

The following information is obtained from the records of the company:

Total standing timber acquired at inception of company:

	Feet	Cost per M feet	Total cost
Yellow fir	700,450,000	$4.00	$2,801,800
Hemlock	300,200,000	1.20	360,240
Cedar	48,600,000	4.00	194,400
Spruce	113,915,000	4.00	455,660
Red fir	75,400,000	2.50	188,500
	1,238,565,000		$4,000,600

Logs cut during the year 1926:

Yellow fir	51,000,000 feet
Hemlock	14,000,000 "
Cedar	1,800,000 "
Spruce	6,810,000 "
Red fir	2,250,000 "

Logs sold during the year 1926:

Yellow fir	45,400,000 ft.	@ $15.00 per M ft.
Hemlock	12,500,000 "	" 12.50 " " "
Cedar	1,800,000 "	" 15.00 " " "
Spruce	4,250,000 "	" 18.00 " " "
Red fir	2,250,000 "	" 15.00 " " "

There was used by the company for the construction of donkey sleds, during the year, 100,500 feet of yellow fir, which is included in the foregoing figures representing the timber cut during 1926. The cost of logs so used for construction purposes is to be added to capital expenditures at the average cost of production of all logs cut for the year, the construction labor cost thereon having been ascertained to be already included in the equipment account.

The inventory of logs "in pond" as scaled (i.e. ready for sale) at December 31, 1926, was as follows:

Yellow fir	5,499,500 feet
Hemlock	1,500,000 feet
Spruce	2,560,000 feet
	9,559,500 feet

The inventory is to be valued at the average cost of all logs cut during the year, no segregation of costs to be made on the various kinds of timber cut.

In addition to the logs cut, as above recorded, there were 500,000 feet of yellow fir logs and 500,000 feet of spruce logs lying in the woods, felled and sawed, and the cost of felling and sawing such logs is included as part of the operating expenses for the year 1926 on the company's books. These logs are to be valued at stumpage cost, plus felling and sawing cost only, as no other costs are applicable thereto.

The railway construction is described in the accounts as main railroad and subsidiary railroad. The main railroad is a completed unit and all the company's standing timber will have to be hauled over that road as cut. The subsidiary railroad is not a completed unit. When completed, the total cost is estimated to be $540,000. The standing timber to be hauled over the subsidiary railroad is 600,000,000 feet. When the timber is all cut both railroads are to be considered as being of no further use and to have no salvage value. Of the total timber cut for the year 1926, 40,000,000 feet were cut from the standing timber adjacent to, and hauled over, the subsidiary railroad.

Depreciation has been provided on all plant and equipment and is to be considered adequate.

An examination of the accounts receivable disclosed worthless accounts amounting to $5,500.

From the foregoing list of balances and supplementary information, prepare the statements desired by the trustees for the bondholders and submit details of the adjustments of accounts considered necessary by you, ignoring income-tax features.

No. 2 (10 points):

Alton, Locke and King are in partnership, their respective capitals and shares of profits being as follows:

Alton	$60,000	40%
Locke	40,000	30%
King	20,000	30%
	$120,000	100%

It is arranged to admit Darwin as a partner with a twenty per cent. interest in the profits, he to contribute as additional partnership capital a sum proportionate to his interest together with an equal amount for goodwill.

(1) How much cash must Darwin contribute in all?

(2) In what proportion will the profits be divided between the four partners?

(3) How should the goodwill be treated?

No. 3 (18 points):

The following communication was received by the National Bank of Extown from one of its branches:

"On April 21st our San Francisco correspondent wired you (the head office) advising you of a deposit made by Byrd & Co. amounting to $2,000 for account of Branch K. The San Francisco bank credited our account (Branch H). You, upon receiving the wireless, credited Branch K and debited San Francisco. On receiving, May 15th, the San Francisco transcript of April 21st, with the credit of $2,000, we debited San Francisco and credited Branch K. Upon receiving advice of our credit to Branch K, they debited us and credited you, under advice of May 17th. Upon receipt of this advice, May 19th, you reversed your entry with Branch K of April 21st by debiting Branch K and crediting San Francisco bank. Now, on June 15th, we receive a debit from San Francisco, dated June 3rd, reversing their entry of April 21st. So, by debiting us on June 3rd, they must have credited you. We have not recorded this debit on our books, awaiting further instructions from you.

"How can this muddle be straightened out?"

Show the entries necessary to adjust the transaction and, incidentally, how all accounts appear after adjustment.

No. 4 (24 points):

Following the close of the year 1926, you are called upon to make a balance-sheet audit for a concern engaged in the manufacture of newsprint and find the following circumstances:

The company was organized the latter part of the year 1913. The plant was completed in 1914 and used for experimental work in developing a new process of paper-making during 1915 and 1916.

The bureau of internal revenue has ruled that the plant started operations on a commercial basis on January 1, 1917.

The original construction cost accounts have been destroyed and the only information relative thereto you find in the following entries as of December 31, 1916:

Plant and equipment	$1,800,000	
Contractors' construction		$800,000
Company construction (Labor and material)		935,000
Damages (Awarded construction laborers for injuries)		20,000
Deficit (1914-15 salary of president and general manager, $20,000) (1914-15 office and administrative expense, 90%, $10,000)		30,000
Profit and loss (1916 salary of president and general manager, $10,000) (1916 office and administrative expense, 90%, $5,000)		15,000

The president and general manager at that time was a construction engineer who devoted his entire time to supervising the construction of the mill. It was estimated, in 1917, that 90% of the office and administrative expenses should be charged to cost of construction.

Plant and equipment	$200,000	
Surplus		$200,000
The S Appraisal Company has placed the replacement value of the plant at $2,000,000 at December 31, 1916.		

Upon inquiry about this entry, the complete appraisal of a reputable appraisal company is placed in your hands.

In September, 1926, the frame superstructure of the machine-room, having become dangerous through decay caused by climatic and manufacturing conditions, was demolished. The brick and concrete foundations and floors were reinforced and a modern concrete and steel superstructure erected thereon which was completed December 31, 1926.

The plant was in operation during construction.

The bureau of internal revenue has allowed 5% per annum depreciation on the correct amount of machine-room construction in accordance with the regulations and *proper* reserves for the years prior to 1926 have been set up on the books. Depreciation on the old structure was entered on the books for the full year of 1926. No depreciation was taken on the new construction which cost $215,000 including $15,000 cost of demolishing the old structure. The bureau will allow 2½% per annum depreciation on the new structure as a unit. The new construction is carried in an account called "Appropriation No. 40" at $215,000.

In the appraisal book, the machine-room construction is summarized as follows:

Frame construction	$72,727.27
Excavations, brick and concrete foundations and floors	109,090.91
Engineering and overhead (10%)	18,181.82
Total	$200,000.00

What entries would you suggest to reflect fully the demolition of the old building and the correct total balance for the new building to be carried on the books? Give full explanations.

What, if anything, would you do with the $200,000 appreciation of plant?

Would your solution of this problem be different if the frame superstructure had been in first-class condition but had been demolished only in the interest of increased efficiency of the plant?

No. 5 (24 points):

A city wishes to buy new fire equipment, costing $500,000, with an estimated life of ten years and no salvage value. It is necessary to issue bonds to pay for this purchase although, at the present time, interest rates are high—six per cent. payable annually.

How would you suggest that these bonds be issued and what would be the annual cost to the taxpayers?

It is expected that a sinking fund would not earn more than three per cent. on the average.

Bonds will be issued in denominations of $100 and multiples thereof.

Given:

$$(1.06)^9 = 1.689479 : (1.06)^{10} = 1.790848$$
$$(1.03)^9 = 1.304773 : (1.03)^{10} = 1.343916$$

Examination in Commercial Law

NOVEMBER 18, 1927, 9 A. M. TO 12:30 P. M.

Answer no more than ten questions as directed
Give reasons for all answers

NEGOTIABLE INSTRUMENTS

Answer three questions.

No. 1.

Boston, Mass.
January 2, 1927.

Ninety days after date I promise to pay to the order of X. Y. five hundred dollars with interest.

(Signed) JOHN DOE
by A. B.
Attorney-in-fact.

Endorsed in blank "without recourse," X. Y.

The above note passes in due course to William Smith. The note being unpaid at maturity Smith sues. John Doe is not liable as maker because A. B. had no authority to sign as agent or attorney-in-fact. X. Y. interposes the defense that he is not liable as he endorsed "without recourse." Is such defense good?

No. 2. On December 1, 1910, A gives to B the following instrument:

January 30, 1911, after date I promise to pay to B four hundred dollars at 25 Broad St., New York, N. Y.

(Signed) A.

B endorsed the instrument to X before maturity for value. A, the maker, did not pay on the due date and defended suit by X on the ground of lack of consideration. Could X recover?

No. 3. Jones, a farmer, owed Smith a sum of money for feed and seeds purchased. Jones, together with his wife, gave a promissory note to Smith for the amount of the debt. In a suit by Smith, the note having been dishonored at maturity, Mrs. Jones defended on the ground that as she was not liable for the goods, the note was without consideration as to her. Was the defense good?

No. 4. By whom must payment of a negotiable instrument be made in order to extinguish it?

CONTRACTS

Answer two questions.

No. 5. A hires an automobile from the Drive-Yur-Self Auto Co. at $1.00 an hour. Through no fault of A the car is damaged in collision with B. Is A liable to the renting corporation? Is B liable to A or to the corporation?

No. 6. Doran, by a written contract, agreed to sell to Best 200 drums of acid of certain specifications, at the rate of 2 drums per diem, title to pass upon delivery. After delivery the acid was to be sampled and tested and the price fixed according to daily market quotations. Best sold his business, including the contract with Doran, to Trimble, but Doran refused to make deliveries to Trimble who thereupon sued Doran for damages. Is Doran liable?

No. 7. What are general damages and what are special damages for breach of contract of sale?

CORPORATIONS

Answer both questions.

No. 8. A banking corporation had a charter giving its board of directors power to alter or to amend its by-laws. One by-law provided that no interest should be paid on certificates of deposit payable on demand. Interest was, however, paid upon such a certificate to X, whom the bank later sued for return of interest. X proved at the trial that he had obtained the written consent of a majority of the directors, one at a time, to such payment. What, in your opinion, should the trial judge have decided?

No. 9. For the purpose of financing a proposed new corporation, what would be the advantage, from the viewpoint of the corporation, of issuing six per cent. cumulative preferred stock (redeemable), instead of six per cent. twenty-year gold bonds?

PARTNERSHIP

Answer one question.

No. 10. Define dormant partner, limited partnership, general partner, trading partnership, ostensible partner.

No. 11. A partner without consent of any of the other partners executed and delivered a mortgage on firm real estate using the proceeds to pay certain firm debts. Was the mortgage binding?

FEDERAL INCOME TAX

Answer question No. 12 and one other.

No. 12. The copartnership of Jones & Smith was declared bankrupt, and copartnership assets were administered by a duly elected trustee. Just prior to distribution of the final dividend to creditors, the internal-revenue department filed proofs of claim against the individual partners for unpaid income tax for prior years, claiming rights to priority of payment under the income-tax-law provision that the bankruptcy court shall order payment of all taxes legally due and owing by the bankrupt to the United States before payment of dividends to creditors. Could the revenue department succeed in its claim?

No. 13. Under the 1926 revenue act, are affiliated corporations required to file consolidated returns? Summarize the provisions of the 1926 act as to returns by affiliated corporations.

No. 14. You are employed as accountant and auditor for a corporation about to engage in an extensive retail business, which will, necessarily, extend credit to a large number of customers. Under the income-tax law, in what way could you treat bad debts?

Examination in Accounting Theory and Practice

PART II

NOVEMBER 18, 1927, 1 P. M. TO 6 P. M.

The candidate must answer all the following questions:

No. 1 (25 points):

From the following balance-sheets and explanatory data, prepare a consolidated balance-sheet.

Submit your working papers relative thereto.

COMPANY X

Balance-sheet—December 31, 1926

Assets

Cash	$20,000
Investment in company Y— 1,400 shares, par value $100	210,000 (1)
Investment in company Z— 4,000 shares, par value $50	200,000 (2)
	$430,000

Liabilities and Net Worth

Current liabilities		$80,000
Collateral gold notes, due 1934		100,000
Capital stock—		
Preferred: 1,000 shares, par value $100		100,000
Common: 10,000 shares, no par value		150,000
		$430,000

Company Y
Balance-sheet—October 31, 1926
Assets

Cash		$60,000
Receivables		100,000 (3)
Inventories		300,000 (4)
		$460,000

Liabilities and Net Worth

Accounts payable		$16,000
Capital stock—		
4,000 shares, par value $100		400,000
Surplus—		
Balance, Nov. 1, 1925	$40,000	
Add: Profit for year	14,000	
	54,000	
Less: Dividends paid Oct. 31, 1926	10,000	$44,000
		$460,000

Company Z
Balance-sheet—December 31, 1926
Assets

Cash		$10,000 (5)
Receivables		40,000 (8)
Inventories		100,000
Investment in company Y—		
800 shares, par value $100		120,000 (6)
Investment in company X—		
250 shares, preferred, par value $100		25,000 (7)
Land, buildings and equipment, as appraised by General Appraisal Co., Dec. 31, 1926, at sound value of		113,000
		$408,000

Liabilities and Net Worth

Accounts payable		$133,000
Capital stock—		
4,000 shares, par value $50		200,000
Surplus—		
Balance, January 1, 1926	$100,000	
Deficit for year 1926	25,000	75,000
		$408,000

NOTES:

(1) Purchased October 31, 1926, at $150 per share.
(2) Purchased January 1, 1926, at $90 per share.
(3) Includes $20,000 due from Z company.
(4) Includes $50,000 goods purchased from company Z.
(5) After remitting $25,000 to company X, which is in transit.
(6) Purchased October 31, 1926, at $150 per share.
(7) Acquired at par.
(8) Includes $25,000 advanced to company X.

No. 2 (21 points):

The Golden Fleece Knitting Mills, engaged in the manufacture of woolen sweaters of various kinds, is in need of financial assistance in order to negotiate some heavy purchases of raw material for the coming season.

The company presents the following statement of assets and liabilities, as at October 31, 1926, with the request that you certify it.

Upon ascertaining the facts as set forth hereunder, make such adjustments as you think necessary and submit a revised balance-sheet showing the ratio of current assets to current liabilities and express your opinion as to the financial condition so indicated.

Assets

Cash in banks and on hand		$10,600
Trade debtors	$95,200	
Less: Reserve for losses	9,100	86,100
Due from officers and employees		5,300
Inventories:		
Raw material	93,000	
Work in process	55,000	
Finished goods	225,000	373,000
Investments—miscellaneous		20,000
Machinery and equipment	95,900	
Furniture and fixtures	20,600	
	116,500	
Less: Reserve for depreciation	21,900	94,600
Prepaid insurance		2,200
		$591,800

Liabilities

Notes payable	$140,000
Accounts payable	40,900
Wages accrued	15,600
Taxes accrued	21,000
Interest accrued	5,000
Capital stock	350,000
Surplus	19,300
	$591,800

Upon investigation, you discover that:

(1) The mill operates under a system of "standard costs" using a basic price for wool yarn of $2 per pound. The standard costs for labor, overhead, etc. vary according to the article manufactured.

(2) The company is granted a discount on yarn purchases of 5% off market prices if paid within 30 days from date of invoice, and this discount is handled on the books as a financial income at time of payment of invoice, not as a reduction in cost of raw material.

(3) The market price of yarn, October 31, 1926, was $1.85 per pound.

(4) The inventories were composed as follows:

Raw material (yarn)	
20,000 lbs. at cost, $1.95	$39,000
30,000 " " ", 1.80	54,000
Work in process—	
Yarn at standard cost, $2.00	50,000
Labor and overhead (standard costs)	5,000
Finished goods—	
Yarn at standard cost, $2.00	200,000
Labor and overhead (standard costs)	25,000

(5) Owing to sundry imperfections necessarily and continually arising in the manufacture, some of the finished articles have to be classed as "seconds" and are sold at 25% less than the selling price of "firsts."

(6) The selling price of "firsts" is 150% of standard cost.

(7) The total production of the mill for the year (both groups being priced at the same standard cost) was "firsts" $680,000, "seconds" $160,000. The inventory of finished goods (as above) contained "seconds" to the value of $60,000 at standard cost.

(8) There were no unpaid bills for yarn included in the accounts payable.

(9) Under a two-year yarn-purchase contract, you find that a shipment of yarn containing 10,000 pounds at the contract price of $1.95 per pound f. o. b. factory or shipping point, left the factory by rail on October 28, 1926, reaching your client on November 5, 1926, with a freight charge of $350. The liability for this merchandise did not appear on the books of the client.

(10) The investments include liberty bonds $3,000, which represents both cost and market value thereof, and also miscellaneous stocks $17,000 at cost, which are not readily realizable and for which no market quotations can be obtained.

No. 3 (20 points):

From the statements following, submitted by Brown & Jones (a copartnership) conducting a retail grocery store, prepare a profit-and-loss account for the year ended December 31, 1926, and the capital accounts of the partners who share equally in the profits:

Balance-sheets—December 31, 1926 and 1925

Assets

	December 31 1926	December 31 1925
Current:		
Cash	$10,500	$7,500
Customers' accounts receivable	55,000	51,000
Inventories	105,000	90,000
Total current assets	$170,500	$148,500
Prepaid:		
Insurance and real-estate taxes	$2,500	$2,250

	December 31 1926	December 31 1925
Fixed—at cost, less depreciation:		
Real estate	$15,000	$10,000
Buildings	55,000	57,000
Equipment	9,000	10,000
Motor vehicles, etc.	10,000	12,000
Total fixed assets	$89,000	$89,000
Total assets	$262,000	$239,750

Liabilities

	1926	1925
Current:		
Notes payable—bank	$50,000	$40,000
Trade accounts payable	15,000	10,000
Manager's bonus	2,000	1,000
Total current liabilities	$67,000	$51,000
Capital:		
John Brown	125,000	104,000
David Jones	70,000	84,750
Total capital	$195,000	$188,750
Total liabilities and capital	$262,000	$239,750

Cash receipts and disbursements, year ended December 31, 1926

Cash on hand—December 31, 1925	$7,500
Receipts:	
Customers	500,000
Rent of apartments above stores	2,000
Suppliers—allowances on defective goods	750
Haulage, etc.	1,500
Notes payable discounted	90,000

Disbursements:		
Wholesalers		$400,000
Wages of store assistants		15,000
Wages of drivers		7,500
Miscellaneous expenses, including telephone, etc.		6,000
Manager's bonus—year 1925		1,000
Notes payable		80,000
Discount on notes payable		3,450
Insurance and real-estate taxes		3,000
John Brown		15,525
David Jones		51,275
Real estate purchased		5,000
Motor vehicles purchased		3,500
Cash on hand—December 31, 1926		10,500
	$601,750	$601,750

No. 4 (14 points):

You are requested by Mr. John Blank, owner of all the capital stock of the Hoffbloom Realty Company, to review and comment upon the statements prepared by his manager, and herewith presented, directing special attention to the item "Net profit to common stock" shown in the second of the two statements:

HOFFBLOOM REALTY COMPANY

Tentative profit-and-loss statement and balance-sheet, December 31, 1926

Assets

Goodwill				$10,000.00
Contracts receivable			$32,880.88	
Other current assets			36,035.54	68,916.42
Deferred expense				4,000.00
Total assets				$82,916.42

Liabilities

Liabilities				$28,081.77
Surplus account and profits—				
Accrued profits, per surplus account			$13,872.22	
Allocated surplus—Reserve for income tax			237.03	
			14,109.25	
Reserve account—Reserve for lot-sale contracts		$89,873.73		
Less: Real-estate accounts—				
Land	$26,608.00			
Development expense	32,540.33	59,148.33	30,725.40	
Estimated total profit to date, contingent upon full payment of lot-sales contracts and no further expense			44,834.65	
Capital stock—common			10,000.00	54,834.65
Total liabilities				$82,916.42

Tentative realization and liquidation statement, December 31, 1926

Assets to be realized—		
Sale price of remaining lots..................	$16,800.00	
Current assets, per balance-sheet.............	68,916.42	$85,716.42
Reserve account—		
Reserve for lot-sale contracts................	89,873.73	
Less: Real-estate accounts..................	59,148.33	30,725.40
		116,441.82
Liabilities to liquidate, per balance-sheet.....................		28,081.77
Net profit to common stock—to pay face of stock and as profit...		$88,360 05

Upon inquiry, you gather the following information:

Goodwill account was opened as an offset to capital-stock account.

The balance in "Reserve for lot-sales contracts" is the result of crediting the account for all sales and, subsequently, charging amounts (transferred to income) proportionate to payments on contracts.

The "land" and "development" accounts contain the total amount expended on "Hoffbloom addition" which the company was organized to plat and sell.

There is considerable expense yet to be incurred, but there is also income (interest on contracts) which may be treated as, roughly, offsetting the expense.

It is expected that the remaining lots will be sold and that all contracts will be paid off within five years from December 31, 1926, when the company will liquidate.

No dividends have been paid on common stock, but on preferred stock, which was retired in 1926, approximately $9,000 dividends were paid.

Prepare a report, in letter form, for your client, embodying therein a criticism of the statements submitted.

No. 5 (20 points):

A, B, C and D form a syndicate for the purchase of coal mines owned by A, for the purpose of selling them to a new corporation, The Northern Coal Company.

This corporation is formed with a stock capital of $2,250,000, composed of 20,000 seven per cent. preferred shares of $100 each and 2,500 shares of common stock of $100 each.

The subscribers pay cash in full for 3,500 preferred shares, B paying for 1,500 shares, C for 1,000 shares and D for 1,000 shares.

The remaining 16,500 preferred shares and also the 2,500 shares of common stock are to be transferred by the company to A as the purchase price of the properties.

The agreement made by the members of the syndicate among themselves is that A is to keep 3,000 preferred shares as the actual price of the properties; that he is to transfer, as gifts to B, C and D, one preferred share for each share paid for by them and to donate to the corporation 10,000 preferred shares which are to be sold and the proceeds credited to surplus account. He is, further, to donate to the syndicate the 2,500 shares of common stock which he received.

A market is to be made for this common stock, and when it is sold the net proceeds are to be divided, as promotion profits, among all the members of the syndicate in proportion to their final holdings of preferred stock.

The common stock realized an average net price of $90 per share. The preferred shares, donated to the company, realized an average net price of $102 per share.

Prepare the accounts of the syndicate, showing the distribution of profit on the sale of the common stock; and prepare the balance-sheet of the corporation after the sale of the donated stock.