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Accounting from the Business Slant

IT would probably sound incongruous to say that accuracy is the curse of accounting. Yet, viewed from a certain angle, there is something akin to sense in the suggestion.

There are still many persons whose idea of an accountant is that he is quick and clever at figures. Many business men still judge financial statements on an artistic basis, stressing particularly the point of accuracy.

With many accountants accuracy and technical presentation are fetishes, the worship of which warps their sense of proportion and interferes with a common sense perspective.

Again, it may seem strange to reiterate what has been enunciated before; that no balance sheet or income statement is ever accurate. The findings are said, and often certified, to be correct, but after all the degree of accuracy is one that is relative rather than absolute.

The important thing about any statement is the information which it conveys, and the significance which the information has. Financial statements are but a medium for the expression of conclusions derived from a scheme, known as accounting, for recording, classifying, grouping and arranging the financial data incident to business.

Accounting is, therefore, but a means to an end; an adjunct or tool of business; a device for furnishing information. It appears, consequently, that the data which accounting produces and reflects by means of financial statements should be regarded in the light of its business significance rather than reviewed from the standpoint of precision and form.

What is the position of the company as an investment enterprise; in its relation to creditors; from a liquid standpoint; with respect to tax liability; as to proper proportions between fixed and current assets, and owned and borrowed capital? What are the tendencies indicated by these factors when compared with conditions existing at a previous date? What relation do the costs, expenses, and charges, and gross and net profits, bear to sales; net income to capital invested? How many times was the bond interest earned? How much per share was earned on the various classes of stock? What was the turnover of merchandise stock; of capital; the relation of sales to plant? How do the classes of expense stand within their respective groups? How do all these things compare with preceding periods?

Such is the information which helps business men to administer intelligently, not a prominent display of some item of deferred expense or accrued salary, computed with painstaking accuracy and inserted in an attempt to be precise, but wholly insignificant in the light of total assets and liabilities, and of no particular interest to anyone.

The progressive business man looks at financial statements always from the business slant. He is not as concerned with what the statement is as what it means and what it indicates to him he should do or refrain from doing. The proper function of accounting is to furnish the financial facts of business. But any accountant who becomes so absorbed in the technicalities of his work as to overlook the business slant misses fire completely.

The Danger in Book Inventories

THERE is perhaps no one item on the balance sheet with so many ramifications which are of interest as inventories. In many industries the inventories are among the most important assets with which the business is carried on. Frequently they represent a large portion of the capital investment. As a consequence of these facts the value at which the inventories are shown may have a marked effect on financial condition.

The term *inventory* signifies stock-taking and implies that the physical property to which the title relates has been counted and listed. Seeing the word *inventories* on a balance sheet one is entitled to assume, unless some qualification appears, that the values shown are based on a physical count.

Given this condition, wherein obsolete, unusable, or unsaleable items have been either excluded, or priced at not more than recovery value, the next question becomes one of valuation. While there are exceptional cases, like the packing industry, where sales prices are used consistently, the well-settled valuation practice is cost or market, whichever was lower at the date of inventory. Orthodox procedure, such as the foregoing, would offer little ground for technical criticism so long as the books had been adjusted to make stock records conform with the physical condition and the adjustments had been applied to the costs. True, there would be questions from the standpoint of management as to relations between inventories and production requirements, and as to the proper balance between capital tied up in inventories and total working capital, etc., but that aspect is beyond the purview of this discussion.

What does call for technical concern and critical consideration is the situation wherein closings are based on book records and inventory values derived therefrom are used for balance sheet purposes. The ground for concern is found, first, in the possibility that there may have been wide divergence between the book records and the physical stock; second, that cost may mean cost when purchased and that some of the stock may have been in hand for a long time, or a fixed price may have been used; and, third, that while physical stocks may have been exhausted several times since the last physical inventory was taken, the book records may not have been adjusted at such times.

Nothing short of an extensive study of the stock records and prices used in figuring costs will serve to determine accurately the fairness of book values used for balance sheet purposes where physical inventories