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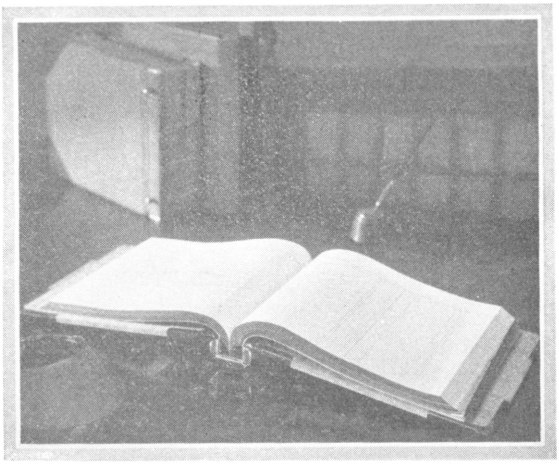

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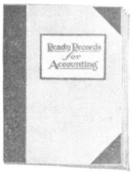

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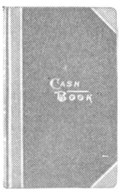

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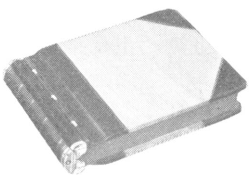

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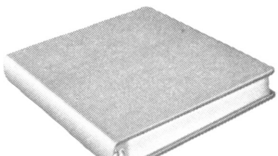

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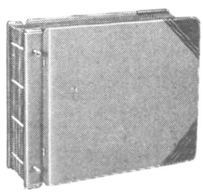

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Principles Governing the Amounts Available for Distribution of Dividends*

BY CHARLES B. COUCHMAN

Stockholders of corporations are a constantly increasing percentage of the people. One reason for becoming a stockholder is the expectation of receiving dividends from the corporation's profits. Dividends, therefore, are of primary interest to stockholders and to the officers of corporations. Principles governing the amounts that may or may not be paid deserve careful thought by all concerned. If the amounts paid out today are larger than they should be, the stockholder of today profits unduly at the expense of the stockholder of tomorrow. If the amounts paid out today are less than they should be, an undeserved benefit passes on to the stockholder of the future and the stockholder of the present suffers unduly.

The various agencies whose function it is to calculate such amounts have not yet reached a degree of skill that will enable them to make accurate determination. There are too many variable and indeterminate factors. Too much of prophetic vision is required to reduce the amounts to exact dollars. Nevertheless some progress has been made. Some pitfalls have been uncovered. Some erroneous methods have been so proved. It is well to summarize the principles that have been established so that advantage may be taken of them and also so that the way may be cleared for further progress.

Principles, to deserve such designation, must be of aid in the determination or expression of truth or must be for the benefit of

* This thesis was considered the best paper submitted by a member of the American Institute of Accountants on the subject *The Principles which Should Govern the Determination of Capital and the Amounts Available for Distribution of Dividends in the Case of Corporations, with Special Reference to the System of Capital Stocks without a Par Value*, and the author was awarded the prize offered by the American Institute of Accountants Foundation.

parties concerned or the community as a whole. With regard to dividends, the parties at interest are the creditors and the stockholders, both of the present and of the future. The rights and interests of all, particularly of the commercial community, must be recognized in defining principles governing the distribution of dividends.

Dividends, other than so-called capital-stock dividends, are either a repayment of investment or a distribution of accumulated ownership in excess of investment, known as earnings or profit. It is with dividends representing distribution of such earnings or profit that the investing world is chiefly concerned. The determination of the amounts available for such distribution with regard to any corporation involves (1) the measurement of such earnings or profit, and (2) the limitations upon such distribution imposed by law, by economic conditions or by managerial policy.

Statutory law enters into the matter only for the purpose of determining and protecting the rights of each party directly concerned and of the community in general. Where matters arise, not contemplated or covered in the laws, the efforts of all parties must still be toward the determination and protection of the rights of the parties themselves and the community as a whole. To the extent that they fail in this, commercial enterprises in general and the efficiency of the community capital suffer.

Capital

The measurement of earnings or profits involves a proper separation of investment from accumulated ownership additional thereto. This requires an understanding of capital and its functions in business. In any consideration of capital, it is necessary to indicate very definitely the content and limitations intended by that term. In this discussion we are applying it to the assets of an individual or organization in excess of the amount necessary to liquidate liabilities to creditors.

No single and exact definition for this term is at present accepted in the economic, commercial and legal worlds. In its broadest usage, it applies to property utilized, not for direct consumption, but rather as an aid in the production of additional property. Such usage, therefore, practically includes all assets of a business, not only those directly owned but also those elements representing property advanced to others or receivable from others. In such a usage there is evidently a duplication, as property held by one organization, but owing to a second, would by such usage be included in the capital of each. The commercial world has attempted to eliminate such duplication by excluding from the capital of each organization that portion of the assets owed to other parties. A deduction, therefore, of the amount of liabilities of any commercial unit from the total assets of that unit leaves what is known as accounting capital, or, in more modern usage, "capital." This is in accordance with the content and limitation expressed above.

A and B have businesses in each of which exactly $10,000 of property is invested. A advances $3,000 of his property to B. A's investment in his business remains the same. In lieu of the property advanced he records a claim against B as an asset for the same amount so that his assets still total $10,000. B, on the other hand, now displays $13,000 of assets under his control, the property received from A being added to the property previously in his possession. An addition to the assets, properly shown by each, gives a total of $23,000 instead of the total of $20,000, which would have appeared prior to the advancing of value from one to the other. One can not say, however, that the combined capital of the two is now $23,000. Such a statement would imply the actual creation of capital by the simple maneuvre of one party lending to the other. Instead, the capital of each remains the same. That of A is expressed by the amount of his assets as he has no claims of creditors to deduct. That of B is represented by the $10,000 of assets in excess of the amount necessary to pay his creditors. The accounting definition and the economic definition of capital are therefore not greatly at variance.

Capital, then, is not a single positive thing. Rather it is the difference between two things of opposite effect. It is a remainder —or rather, it is the measure of a remainder in which a certain fund of assets is the minuend and the claims of creditors are the subtrahend. The value of capital must depend upon the measure of these other two things.

The value of capital at any moment depends also upon conditions. Assets of a corporation continuing and expecting to continue according to the plans for which it exists may be worth one amount, and the capital may be determined by using that amount as a base. The assets of the same corporation facing dissolution or sale to another organization may be worth a far different amount. The capital as determined from this base may differ greatly from the capital as determined in the first instance.

Again, the amount of capital, being once determined at a particular instant, may change in the next. A sale for three dollars of that which cost in total two dollars adds a dollar to the capital. The breakage of a wheel or a slight turn of style or invention may decrease it. An overnight change in commercial affairs may add to it or subtract from it. It is as erratic as a homeless sheet of paper in a windy alley.

Capital can not be adjusted directly by all these flickering amounts. Thus, preferably, they are all accumulated in accounts over a period of time—some accounts favorable, some unfavorable —and, at the end of the period, all these accounts, each having accumulated during the period the total of some kind of effect, are all brought together—those showing increases of capital being offset against those showing decreases—and the net is amount added to or deducted from the capital. Thus profit is not only measured but also analyzed.

The assets resulting from profits are not tagged or earmarked, as some optimists fondly think, but instead are merged with the other assets of the corporation, as the assets contributed by stockholders and those advanced by creditors may be merged inextricably. As a result all assets must be measured and the liabilities deducted to determine the amount of accounting capital. Similarly, from this amount the portion representing original investment must be deducted to determine the amount of profit accumulated thereon. These measurements being duly made become a basic part of the accounting records, all changes being given effect therein as they occur. This measuring is at present indicated in terms of moneys. No allowance is made for variation in the effectiveness of the money units at various periods of time. This phase of the matter we desire to discuss later.

Let us first give consideration to the measurement of assets. This term is in such common usage that it is tossed about freely by all kinds of business men, used in a variety of bùsiness statements, discussed by congressmen and courts, and yet withal, despite the familarity with which it is treated by these various individuals, there is a sad lack of uniformity in their concepts with regard to it.

In its professional use, the term is gradually becoming more definite. All elements rightfully included in such professional definition may be divided into classes, the principles governing the measurement of each being recognized more fully as experience proves their truth.

The measurement of liabilities is simpler and is more definite than that of assets. It is the amount of moneys necessary to liquidate all claims of creditors at the date of measurement, so far as it may be determined.

If we would know accurately the increase of assets above the sum of the amounts advanced by proprietors and the amounts advanced by accrual to creditors, it is evident that we must maintain such a record that these increases may be accurately determined. We must, therefore, first, maintain a record of the amounts of assets so advanced as capital and advanced by creditors and, secondly, we must properly record the increase, with such proofs as will eliminate errors as far as possible. If this point be kept in mind it makes definite the methods which we must use in the recording of asset values. These methods vary with the character of the assets. For this purpose all assets of a corporation may be divided into five groups, as follows:

1. *Cash* includes money and items directly convertible into money by demand upon financial organizations. The measure of this group, so far as this country is concerned, is self-expressed to the extent that it consists of dollars. If all or any part of it consists of moneys of other countries these must be measured by the accepted ratios of exchange.

2. *Claims to be collected* include all legally enforceable claims upon other commercial units for definite amounts of money. This group is measured on the basis of the number of dollars expected to be realized therefrom.

3. *Assets to be sold*, not having as yet produced any profit, must be valued at what they have cost, less any loss due to decrease in market price. They may not be distributed at any higher amount without involving a negotiation equivalent to sale. Possible profit upon them must not enter into the records until sale or contract has actually created either cash or a legal claim for cash.

4. *Assets to be used*, which are intended to be of service in the creation of profit, should be valued at the amount of capital outlay which they represent, less such portion thereof as represents expired use—namely, amounts measuring the portion of

the service applicable to past periods which presumably has been recovered by charging the gross income of those periods.

5. *Items considered as assets* in the sense that they represent a capital expenditure but are not to be sold nor used nor collected—such as organization expense—if valued at the outlay which they represent and no portion of them is charged as expense or loss over the ensuing periods do not affect the amount of net profit. Any reduction in such amount representing original outlay results in a corresponding reduction of surplus or profits for purposes of distribution.

It may be noted from the above that profits are created normally only by sales or income represented by the first or second of the above groups. The amount of such sale or income is decreased by the used portions of the third and fourth groups. Any dividends therefrom presumably represent amounts which may be taken out of the corporate fund and distributed to stockholders without handicapping any of its activities and without reducing the fund which under the law is to be held for protection of creditors.

Protection to Creditors

If creditors are not properly safeguarded, the operation of credit is injured and the approach toward maximum efficiency of capital use—which is one of the goals of society—is delayed correspondingly. Similarly, if present stockholders are favored unduly, the corporation suffers with resultant loss to future owners, whether they be the same in personnel as at present or not. The present stockholders are deceived as to their true income. Their business judgment is handicapped in its functioning by being given false data from which to judge.

In order that the economic capital of the world may be used with any degree of efficiency, it is necessary that there be free movement of capital between organizations. If one commercial unit can use a certain amount of capital additional to its own, there must be some scheme whereby that amount may be advanced by those having such amounts available who will profit by such a loan of value. This involves the whole great scheme of credits whereby a form of coöperation between organizations is effected in the utilization of capital. Here is a theme that might be expanded indefinitely.

In order that one organization may be justified in thus advancing values to another, it must have some protection against shrinkage of the assets advanced and put under the control of the other party. Such security is usually obtained or sought by giving the one making the advance a general lien on all the assets of the debtor not previously and specifically pledged.

It is a well established fact in the economics of finance that a creditor can not advance values to any organization unless that organization has other values which may serve as a sort of collateral or guaranty of its ability to return to the creditor at maturity date the amount advanced. All assets are subject to shrinkage. The assets advanced by a creditor may shrink to such an extent that he is ill protected unless the debtor has other assets and the shrinkage will not affect his ability to pay his debts. The creditor automatically must have a lien upon the assets of the debtor. In the case of sole proprietorships and partnerships this lien may be applied through proper legal procedure whether the assets of the proprietorship remain in the business or are withdrawn. A partner may transfer certain assets from the partnership fund to his own fund, but the latter is still presumably accessible to the creditor if necessary for repayment of advances.

In the type of organization known as a corporation, the state builds a fence around the fund of assets. Creditors of the corporation can not cross this fence into the private fields of the individual stockholders save in certain cases not necessary to discuss in this argument. It is therefore evident that no creditor would advance a value to a corporation unless there were retained within the fence some assets of the proprietorship which would be subject to the creditor's lien in case of necessity. If corporation stockholders could withdraw all assets save those advanced by creditors there would be no such protective fund. The state, therefore, has so constructed the fence that not only is the creditor forbidden to cross it to reach the fields of the private stockholders, but, further, the private stockholder is forbidden to cross it for the removal of any assets of the corporation, save those in excess of the amount stipulated as a fund which must be maintained for the benefit of creditors. In the early forms of corporation this fund was the amount of the par value of the capital stock. This fund might be lost through business operation without the stockholders being compelled to replace it; but no part of it could be paid to the stockholders as dividends so long as the rights of creditors might be jeopardized thereby.

In order that this principle may be adhered to, it is necessary that accurate methods for measuring profits be used by corporations so that the amount of accumulated assets in excess of those represented by liabilities plus the amount of this fund as required by statute may be accurately determined. In the determination of the amount available for distribution to stockholders due attention must be given to this legal limitation.

Attention must be called to the effect which the reacquirement of stock may have upon this limitation. If treasury stock so reacquired is carried as an asset, there may be no evidence of the fact that a certain portion of the paid-in capital has been paid out again to stockholders and that the fund supposed to be maintained for the benefit of creditors has been correspondingly reduced.

Economic Limitations

In addition to legal limits upon the amount of accounting capital that may be distributed to stockholders there are practical economic limitations. Perhaps the first of these is the question of availability. Profit legally unhandicapped may not be available because of its nature or source or because of being impounded. If profits are in the form of receivables or inventories or other similar assets, there may be no satisfactory method of making distribution to stockholders.

Assets to be distributed evidently must be in a form that will permit physical removal from the fund of a corporation without handicapping that corporation's operations. Such assets may be created as the result of sales of commodities or service for an amount in excess of cost. These sales will result either in cash or in receivables ultimately convertible into cash. All this cash in excess of cost represents a realized profit and it is apparently only out of such realized profit that dividends are justifiable. Moreover the commodities or service sold must be such that the sale will not decrease the efficiency of the organization. To be available for dividends, therefore, assets must not be of a character which renders them necessary for the carrying on of the activities of the corporation. It is evident that no asset amount, merely created by appreciation of permanent assets, can be used in the payment of a dividend; nor should any such amount be allowed to appear as though it were a profit until actually realized. To encumber the figures, which are supposed to measure the amount of profit, with fictitious asset values merely beclouds one of the fundamental functions of profit-and-loss statements. On the other hand, the failure properly to recognize the expired portion of an outlay for such fixed assets would result in understating those costs which must first be subtracted from gross income before the amount available for distribution is determined.

Frequently corporations feel that their permanent assets have so increased in value because of the general trend of prices that they are justified in reducing to a minimum the amount of depreciation which they charge periodically against income. This understatement of the item depreciation results automatically in an overstatement of net income and, therefore, an overstatement of the amount of profit from which dividends may be declared. To pay out such an amount of income as dividends results in a distribution based upon an alleged increase in the value of a permanent asset and violates the principle which we have attempted to explain. Economically such a procedure is unsound. If carried to the extreme it would seriously handicap the activities of a corporation. The cost of fixed assets for use or service must therefore be construed as merely prepayments for such service. This prepayment must be distributed over the years of service in such a manner that at the expiration of the service there will have been withheld from gross income an amount known as depreciation which, together with the recoverable value or scrap or salvage value of the asset, will equal its original cost price. If a less amount is withheld, a portion of the original cost will not have been provided for and will have been merged with the net income and thereby have been added to surplus. If such surplus has been distributed to stockholders the organization will have violated the original legal limitations upon dividends discussed earlier in this article.

Corporations frequently find it necessary or desirable to retain a portion of otherwise available profits in order to meet the needs involved in expansion or provision of efficient facilities or to meet some liability or expected loss. The policy of conservatism dictates such withholding for the good of the organization and therefore for the good of its stockholders individually. To carry this policy too far, however, results in withholding from the individual stockholders that which is rightfully theirs. For the corporate officers to assume that by retaining assets they are really using them more advantageously for the benefit of the stockholders than the latter could use such assets if put into their possession smacks of corporate paternalism. Retaining funds in excess of proper needs is equivalent to compulsory re-investment. The economic rights of stockholders may be invaded by such action even though they may have no legal redress.

Directors of a corporation may be bound by contract to retain certain amounts of profits in order to comply with the sinking-fund requirements of bond issues. With regard to other amounts to be appropriated they have the legal right to use their discretion. Stockholders have a right, however, to be kept informed as to such appropriations, for they really represent the informal re-investment of an earning, without so much as the issuance of a certificate to identify it.

It is desirable to have all limitations with regard to profits expressed in the accounting records so that balance-sheets prepared therefrom may display the accounting capital in such a way that the observer will have some guide as to the amounts of surplus available for distribution as dividends. The legal limitation is usually expressed by the amounts of the capital-stock accounts if the stock has a par value. The economic limitations or those adopted as part of the policy of the corporation management may be expressed through accounts designated as surplus reserves or appropriations, such as "sinking fund reserve," "surplus appropriated for new factory" and "reserve for contingencies."

There is one economic limitation upon profit distribution with which everyone is familiar, and yet it is continually and persistently ignored in business records. That is the fluctuating power of the money unit. One dollar today is considered on the records the same as one dollar of twenty years ago. A corporation that invested $100,000 then shows an accounting capital of $150,000 now and we say it "has accumulated $50,000 of profits." Perhaps it has accumulated no profits at all. Perhaps the equipment and working capital it has today are even less efficient than those it had at first. No part could be distributed without actually distributing that which is the equivalent of original investment. Such a distribution would in reality be a liquidating dividend and not a profit dividend.

If the investment of the stockholders of a corporation is sufficient for all its operating needs, any earnings above this amount, after allowing for taxes, for depreciation and for other portions of expired investment, should be available for distribution to the stockholders. Theoretically this is correct, but practically it can seldom be followed. An amount of capital sufficient for the needs of a business one year is seldom sufficient for its needs the following year. More or less of the profit must be retained in order that business may be developed and efficiency of operation be increased. Because of the constantly decreasing effectiveness of the monetary dollar the number of dollars in effective representation must be continually increased as each part of the equipment is replaced. The replacement to produce equal effectiveness requires a greater number of dollars than did the old part which was removed. As a result it is seldom true that an organization having a net investment of $100,000 in 1913 and also $100,000 in 1923 has held its own, save for the dividends that may have been distributed. To express this differently, if the organization has paid out all values during this period over and above those measured by 100,000 of dollars it has actually distributed a portion of its original capital. There are exceptions, but in many cases the truth of this statement is evident. If the organization in 1923 owns the identical assets that it owned in 1913 the fluctuation in the measuring content of the dollar does not affect their condition. If the assets in 1923 differ from those owned in 1913 and consist of assets whose price has greatly increased in that ten-year period, it is self-evident that the effectiveness of assets costing $100,000 at the latter date would be much less than that of assets costing a similar amount in 1913.

This is an element frequently overlooked by corporations and, for that matter, by accountants. Whether or not the business world is ready to accept a modification in the systems of accounting which have prevailed in the past, we are considerably in doubt. Whether or not the accounting profession is able to offer a practical method of overcoming the difficulty is a still more doubtful matter. Whether or not the future will bring forth a practical solution remains to be seen. Meantime the problem is one vitally affecting the economic structure of commerce and one not wholly to be ignored.

No-Par Stock

The introduction of capital stock without par value brings new complications. It is doubtful if there has yet been a sufficient legal interpretation of the relation of no-par stock to the protection of creditors. States authorizing the issuance of capital stock with no par value usually require designation of a certain amount per share which must measure assets withheld from distribution. Usually, however, this amount per share is very small. It would seem that creditors of corporations whose capital stock consists entirely of the no-par issue would be greatly concerned with this item. Assume a corporation authorized to issue 100,000 shares of no-par stock with a nominal value of five dollars a share required under the statute. If this stock be issued for, say, an average of $20 a share so that capital stock appears on the balance-sheets at $2,000,000, the question arises to what extent creditors should be influenced by that figure in the granting of credits. If the directors choose to distribute to the stockholders a portion of this $2,000,000, still maintaining the fund of $500,000 required by the state, have they violated the rights of creditors? Have the creditors any recourse under our present laws? To express this differently, is it proper to construe any amount paid in for no-par stock, in excess of the nominal value as indicated in the statute controlling the corporation, as paid-in surplus, the same as amounts paid in excess of the par value of stock whose certificates express such par value on their face?

The introduction of no-par stock into the realm of business is so recent and the problems resulting therefrom in many cases have been so unexpected that it is not astonishing that many principles have not yet reached a satisfactory development either in law or in practice. There is as yet little uniformity even in the methods of recording its issuance and its reacquisition. Many of the methods in use fail to give effect to facts necessary to a proper consideration of the question of dividends.

The original issue of no-par stock may be carried upon the records of a corporation (1) at the amount of the accounting capital applicable to such stock, or (2) at the value of the assets for which it was issued or (3) at the amount representing the statutory minimum of the state under whose non-par stock laws the stock was issued. Under the second and third methods surplus accounts must be used to absorb any excess of capital accumulated above the amounts expressed by the capital stock. The first method, although seeming to conform closely to the original idea back of the law creating stock without par value, still fails to satisfy the commercial world. It measures in one account the capital applicable to the stock of no par value, whereas portions of that capital may differ greatly from each other as to source and as to availability for distribution. Economic principles necessitate a separation of the amounts measuring values contributed by proprietors to a corporation from those amounts measuring values accumulating to the credit of the proprietors as a result of corporate operation. This separation should be indicated upon the accounting records.

The second method indicated above provides for such separation. The amount expressed as no-par capital stock indicates the value of the assets received by the organization from the stockholders. Additional amounts accruing to the owners of stock are displayed in a separate account or accounts. The latter accounts are presumed to represent surplus available for dividends unless some portions thereof have been appropriated to meet expected needs for expansion, liabilities or unusual losses.

The third method apparently has little justification. Under such a method any amounts paid in for stock of no par value in excess of the minimum amount per share stipulated under the no-par stock statute would appear as a sort of paid-in surplus or would be merged in the general surplus. Under the latter treatment no separation is made between values contributed and other values earned by the corporation.

Methods of recording no-par stock that is reacquired by the issuing corporation vary even more than the methods of recording original issue and are dependent somewhat upon those methods. If the original issue is recorded at the minimum required by statute, as discussed under the third method above, presumably the reacquired stock should be recorded in like manner. Any amount paid for such stock in excess of the amount per share at which it is recorded will evidently represent a decrease of surplus. If the amount per share of surplus so paid out is in excess of the amount per share applicable to the remaining outstanding shares it would seem that the rights of the remaining stockholders have been injured. Also, if this amount is in excess of the amount paid in as part of the purchase price of such shares when originally issued, it is evident that a certain portion of accumulated profit has been paid out to the holders of these shares. Unless the accounting records have separated amounts paid in for stock from later surplus from earnings they will fail to indicate that earned surplus has been paid out to the owners of these shares.

Such a failure would violate accounting principles, economic principles and perhaps legal principles.

If the original issue of no-par stock has been recorded at the value of the assets for which it was issued, as noted in the second method above, the reacquired stock should presumably be so recorded as properly to offset such entry. Two methods are used in the attempt to accomplish this purpose. Under one the reacquired stock is entered at the price originally paid in for the identical shares when issued. Under the other method the reacquired shares are recorded at the average price which has been paid in for all shares of the same class of stock, without attempting to identify the amount paid in for the particular shares reacquired.

To illustrate this point simply, assume that a corporation authorized to issue 2,000 shares of no-par stock issues the first 1,000 at $10 a share and begins operations. The possibilities of profit are developed to such an extent that at a later date 1,000 additional shares are issued for $20 a share. If the capital-stock account be carried at the values for which the stock is issued it will now appear with a balance of $30,000. If 500 shares are reacquired they may be recorded at $15 a share, this being the average of the stock outstanding at that date. Or they may be identified as being a part of the first 1,000 or a part of the second 1,000 and therefore be recorded at $10 a share or at $20 a share, as the case may be. Any excess paid for such reacquired shares above the price at which they are recorded as treasury stock subtracts from the surplus of the corporation. Conversely, any excess of the price at which they are recorded as treasury stock over the price paid for their reacquisition adds to the surplus of the corporation. The remaining stockholders are therefore vitally affected, not only by the price paid for the reacquisition of stock but also by the method of recording the purchase. The principle to be used in making the record must evidently be one that will result in compliance with the principles of law and of economics governing the relations of stockholders to the corporation. It must also result in a proper display of the true interests of stockholders and the surplus rightfully available for distribution to them.

Some organizations reacquiring capital stock of no par value carry it on their records as treasury stock at the amount paid for it. The effect of this is to distort the ratio of surplus to capital stock outstanding. If the reacquisition has resulted in any addition to or deduction from surplus, as discussed above, such changes should be indicated in the surplus account. Further, a deduction of the amount of treasury stock from the amount of stock issued gives the value at which the outstanding shares are carried by the corporation. This amount should represent a portion of the assets not available for distribution to stockholders. That the method is illogical may be demonstrated by illustrations. Assume that the corporation referred to above, whose 2,000 shares of no-par-value stock were originally issued for $30,000, accumulated an earned surplus of $75,000, and found it desirable to reacquire some of this stock. Further assume that the corporation was justified in paying $50 a share for 500 shares reacquired. If this treasury stock was recorded at the amount of the purchase price, $25,000, the effect would be to indicate a net value of only $5,000 representing capital stock outstanding as follows:

Capital stock, no-par value:	
2,000 shares issued	$30,000
Less 500 shares reacquired	25,000
1,500 shares outstanding	$5,000
Surplus	75,000
Total capital and surplus	$80,000

Such a method of recording is evidently absurd. If there were an earned surplus of $75,000, note what the effect would be in the various methods of recording this treasury stock. If the stock were identified as having been originally issued at $10 a share and were so recorded at reacquisition the effect would be:

Capital stock, no-par value:	
2,000 shares issued	$30,000
Less 500 shares reacquired	5,000
1500 shares outstanding	$25,000
Surplus	55,000
Total capital and surplus	$80,000

If the stock were identified as having been issued at $20 a share and were so recorded when reacquired, the effect would be:

Capital stock, no-par value:	
2,000 shares issued	$30,000
Less 500 shares reacquired	10,000
1500 shares outstanding	$20,000
Surplus	60,000
Total capital and surplus	$80,000

If the reacquired stock were recorded at the average price per share of the stock outstanding prior to repurchase, the effect would be:

Capital stock, no-par value:	
2,000 shares issued	$30,000
Less 500 shares reacquired	7,500
1500 shares outstanding	$22,500
Surplus	57,500
Total capital and surplus	$80,000

An analysis of the amount paid in for the remaining outstanding stock and of the relation of surplus to the remaining stockholders discloses that that method is most just whereby the reacquired stock is recorded at the exact amount for which it was originally issued. Owing to the complication arising if stocks are transferred frequently, such identification may at times be impracticable. In such cases recording the reacquired stock at an amount per share determined as being the average cost per share of the outstanding stock prior to the reacquisition seems the nearest to accomplishment of the desired purpose. This is too brief an article to enable one to carry through the analyses to prove this contention.

No method can meet the needs of commerce that does not provide for correct determination of earned surplus and the effects upon surplus of any repurchase of capital stock.

Summary

Presumably stockholders of a corporation are entitled to a distribution of all profits above amounts necessarily withheld for purposes which we have discussed.

It is for the good of the community as a whole as well as for the good of the individual that wealth not needed for consumption should be utilized in producing more wealth and, further, that such increase of wealth should be made available to its true owner with the minimum of delay. Profits retained by a corporation above the amounts necessary for preserving its commercial and financial integrity are the equivalent of a reinvestment of capital by the stockholder without his individual consent. While the declaration of a dividend from profits in excess of the limitations discussed is left to the discretion of the board of directors, the presumption must be that their duty to stockholders is to make such declaration. Failure to do so deprives the stockholder of the control of wealth that has properly accrued to him and to which he is properly entitled.

To summarize, profit distributions may be made by corporations from assets accumulating to their ownership in excess of amounts necessary to liquidate liabilities and amounts received as investment from stockholders, subject to the following restrictions:

First: legal limitations intended to protect creditors.

Second: practical limitations due to the non-availability of sufficient assets in a form suitable for distribution.

Third: limitations imposed because of contract whereby certain amounts of profit must be temporarily appropriated to uses other than distribution, such as the liquidation of bond issues.

Fourth: limitations imposed because of economic conditions whereby amounts additional to original investment must be retained by the corporation to provide for uninterrupted continuity of operations and undiminished efficiency.

Title to all assets representing profits above these limitations should be passed promptly to the stockholder by periodic dividends so that he may use his own judgment as to the proper utilization of wealth accrued to him as the result of his investment which he may desire to use for his own good or for that of others or to re-invest in the same or in some other enterprise.

Cost of Maintaining Depositors' Accounts*

By Frederick H. Hurdman

The subject of costs is usually considered from a technical point of view and any discussion is, therefore, apt to lead into depths far beyond the ability of the average man to comprehend. Fortunately, it does not seem necessary to reach those heights or depths in a paper such as this. If we can arrive at a clear understanding of the basic meaning of costs and their application to the business of running a bank, we shall have accomplished something.

Cost accounting is usually associated with manufacturing. As a matter of fact, few businesses do not, to some degree, harbor the element of cost in relation to the income of that business. For instance, the wholesaler or retailer, if he is to know which lines or departments yield an adequate profit, must resort to costs. In a particular department yielding a gross profit of, say, 25%, some articles may be priced to yield as high as 40% or 50%, whereas others may yield a gross profit of only 15% to 20%. Even the professional man must base his fees with some regard to the cost. A dentist, valuing his services at $10,000 per annum, must resolve that sum into so much per working minute. If he is a prudent dentist he will do the same with the salary of his assistants, rent, telephone, supplies, depreciation of equipment, etc. By adding these two amounts he has a basic cost per minute and, therefore, a basis for his charge to patients with almost a certainty as to net income, provided his preliminary estimate of working minutes in the year is correct.

The basic elements entering into costs consist of material, labor and overhead, or burden as it is sometimes called. There are varying methods of allocating these three elements against the unit for which the cost is desired. The ratios of each element to the other two will vary widely in different lines of industry. In some branches of manufacturing the basis for allocating these three elements to the article for which a cost is desired may be quite complicated and in others simplicity itself.

The development of correct accounting procedure is a slow educational process. The tendency is to rely on more or less

* A Paper read at Convention of New York State Bankers' Association at Montreal, Quebec, June 23, 1924.

haphazard information or intuition as to results to be accomplished. This is probably due to the fact that most business men are essentially manufacturers or salesmen. They are primarily interested in making or selling something. The keeping of records is a necessary evil.

Edward N. Hurley, chairman of the federal trade commission in 1916, who did a great deal to develop the idea of better accounting and cost methods among manufacturers, said:

> An amazing number of manufacturers, particularly the smaller ones, have no adequate system for determining their costs and price their goods arbitrarily. It is evident that there must be improvement in this direction before competition can be placed upon a sound economic basis.

We are prone to look only at the net result and ignore many of the steps leading up to that result. This is especially true if a fairly satisfactory net profit is realized. However, in the present highly developed state of industry, largely as a result of the impetus given to business during the past ten years, it behooves everyone, be he manufacturer, wholesaler, retailer, banker or professional, to set his house in order and provide some means whereby he can follow the trend of his business with a view to strengthening some features and eliminating others entirely.

The banker has something for sale just as truly as the manufacturer. It is admitted that that something consists mainly of services, but it is essential that he should know the cost of those services in order that unprofitable business may be eliminated or made profitable.

As W. H. Kniffin says in his book, *Practical Work of a Bank:*

> Bankers are no longer satisfied to know that they have made a profit—they want to know where the profit came from and how it arose. It is needful that the sources of profit be known in order that the sources of loss be also known. . . . Aside from lending money the bank renders the following service to its depositors: Receives his funds—money, cheques and other instruments of credit on deposit and for collection. The money it keeps safely; the other items it turns into money sometimes without cost. It furnishes him with a cheque book and pass book, free; pays his cheques as he directs; returns the receipted vouchers with a statement rendered; often makes up his payroll; furnishes money in such form as is requested; guarantees that the party to whom the cheque is payable has received the money; and warrants not to pay on forged orders.

If one stops to think what may be the consequences where trustworthy data are unobtainable through lack of an adequate system of accounting, it will be appreciated how necessary it is to any business to have this information. On the other hand, there are many concerns which are relying today on totally inadequate records for the conduct of their business. How many times have bankers preached better accounting methods to customers. Indeed, the accounting profession is very grateful to the banker for the work he has done in developing the field of accounting. Of course, the banker has not been altogether unselfish in this endeavor, as it was greatly to the interest of the bank that its customers keep careful books of account, showing the correct financial status, and maintain some adequate method for ascertaining the cost of doing business. As the customers of a bank prosper and are successful year after year in their business, so only can the bank hope to prosper and keep solvent.

What I am about to say now may appear to come with poor grace as the guest of bankers, but when I recall the many times I have listened to bankers' harangues to the accountant on his shortcomings I may be permitted to make a few observations.

Like the proverbial shoemaker who mended everyone's shoes but those of his own children, I believe it is a fact that, as a class, bankers maintain for their own banks the most inadequate and unscientific systems of accounting that will be found in any branch of industry. This condition is probably due to several causes:

1. Tradition or custom as to general procedure surrounding the banking business;
2. Low salaries paid to bookkeepers and clerks;
3. Non-technical training as accountants on part of officers and clerks;
4. Apparent ignorance of the accounting profession as to routine work in the operation of a bank.

I do not mean to infer that the banking situation in this respect is hopeless. In fact the interest indicated in this question of costs shows, at least, that bankers appreciate that something is missing in the banks' system of accounting. In looking up the available data on this subject of costs it developed that reams of valuable matter have been written and this subject has been discussed at many meetings. Banks have been adopting modern appliances such as bookkeeping machines, addressographs, telautographs, etc., to simplify the procedure and provide a means of overcoming the ever-increasing mass of detail incident to the operation of a modern bank. In the same bank, however, where one will find all these modern appliances, as well as the monthly statement, it will not be uncommon to find:

1. All income and expenses recorded on a strictly cash basis without any statement as to the real income earned or expenses incurred for the period under review;
2. No classification of income or expenses or, if classification is attempted, on so unscientific a basis as to be of little value in a study of the bank's operations;
3. No attempt to allocate income and expenses departmentally for the purpose of determining the efficiency of department heads;
4. The most inadequate method, if any, for determining whether or not the accounts kept by the depositors of the bank are maintained on a profitable basis.

If it is important for the manufacturer or the merchant to maintain an adequate system of accounts to ascertain if any department of his business is being operated at a loss, why is it not just as important for the banker also to do this? There may be some slight excuse for this omission if one is conducting a bank solely on a service basis without regard to dividends to stockholders. I say "slight excuse" advisedly, for, even if banking were conducted on so philanthropic a basis, there would still be the necessity of treating all depositors fairly. It will be conceded, as between two depositors maintaining daily balances apparently of equal amounts, if it could be demonstrated with reasonable accuracy that on one account the bank realized a monthly profit of $100 whereas on the other there was a loss of $100, an injustice was being done, assuming, of course, that we can disregard what might be termed indirect benefits, difficult of valuation, accruing to depositors and stockholders alike.

Few banks, however, are operated on so altruistic a basis that profits can be utterly ignored. In fact, it has been my experience that profits are a most important factor in the development of a successful bank. If that is so, why should not the banker, who is generally looked upon in the community as the source of sound advice, be the first to adopt those methods which he himself believes necessary in a well conducted business?

Are bankers afraid to face the knowledge that the account kept by Mr. Jones is costing the bank several hundred dollars per annum more than is earned on the balance which he condescends to leave in the bank, or are they afraid that if they speak to

Mr. Jones about this condition he may take his account across the street to a competitor? Are bankers very much concerned if he does relieve them of a losing account? Does it not resolve itself strictly into a selling proposition at this point?

A. P. Howard, in his article on *How to Determine the Cost of Accounts in Small Banks or Trust Companies*, has said:

> Human psychology enters into the discussion. Some customers will leave you no matter what your arguments may be. They will not understand you. This state of mind cannot be avoided, but is it not better to lose a profitless account rather than maintain it because of the unreasonable attitude of an individual depositor? It is true that he may tell others about the treatment received and the collateral influence may do your bank some harm. The only answer is that all education and enlightenment is a slow process but invariably it works for the benefit of all. It is the basis of human progress, public education, and is the cornerstone of our form of government. Fear of the results of education and enlightenment can only lead backward.

What would one say to a customer of the bank if he reported that he was losing $2.00 on every pair of a certain style of shoe? The first question would undoubtedly be: How much of that $2.00 loss represented overhead and how much was actual labor and material? The next question would be: How necessary was this particular style of shoe to sales of the profitable styles? On his answers to these two questions would depend the advice as to continuance or discontinuance. I am assuming, of course, that the shoe manufacturer has a good cost system and that he has exhausted every effort to reduce the cost of this particular style of shoe.

While there undoubtedly has been a great deal of interest manifested in recent years by bankers on this question of the cost of maintaining a deposit account, I doubt if many banks make more than a pretense at seeking a solution of this particular problem in their institution. A great deal has been written on the subject, but apparently the thought has been that only the large banks could afford to go to the expense of ascertaining this cost. Until all banks, big and little, realize that costs are an essential part of their regular system, the full benefit to be derived from such a study will not be felt.

How many older bankers remember the day, not so many years ago, when, in fear and trepidation, you asked a prospective borrower for a statement of his financial condition as a basis for a decision on his application? Today if a borrower is not asked to submit such a statement at least once a year, duly certified to by a firm of certified public accountants acceptable to the bank, he feels slighted. You have no fear that he will become irritated by such a request and take his account across the street, because you feel morally sure that your friend Mr. X will ask him the same question.

That, I believe, is approximately the condition you can create with regard to this question of cost of maintaining a depositor's account. True, there will be a degree of variation as between two or more banks in the total cost or net profit for the same account, but a large part of the cost will be so similar that great good should accrue to the banking community by the ultimate unanimous adoption of some more or less recognized basis for ascertaining costs. This can only be accomplished by education. You, yourselves, must be thoroughly convinced of the necessity, then you must sell the idea to your neighbor who may be less willing to see the light.

If the question of costs is fundamental and if it is conceded that cost does enter into every transaction in which there is hope of profit, then surely there can be no argument as to the propriety of costs in the banking business. *Webster's Dictionary* defines cost as

> The amount paid, charged or engaged to be paid for anything bought or taken in barter; charge; expense; hence, whatever, as labor, self denial, suffering, etc., is requisite to secure benefit.

It will be agreed that there is much labor and self denial even if there is little actual suffering in the maintenance of friendly relations with the depositors of your respective institutions.

This relation of bank and depositor is decidedly two-sided, and unless an equitable arrangement is entered into the association cannot endure successfully. For the depositor, the bank acts as his agent in receiving and collecting deposits, by cashing on demand cheques which the depositor draws on the funds so deposited with the bank, by safeguarding those funds, by an allowance for interest and numerous other special services. In return for this the bank, by investing the funds of its depositors, hopes to make more in income than the cost of all these services enumerated above.

An intelligent cost analysis of a depositor's account will disclose whether or not the bank has realized a profit, or whether the account has actually cost the bank money to maintain. The adoption, generally, of a plan of cost analysis should protect not only the bank but the public as well against injudicious competition. No competition is quite so disastrous or difficult to combat as that based upon ignorance.

These benefits will be measured not only by an improvement in the relations with your depositors, but, with the exchange of information between banks as to unit costs of doing particular kinds of business, more efficient organizations will be developed and costs of doing business will be reduced.

Probably the bank's simplest remedy for an unfavorable situation disclosed by the cost analysis will be an adjustment of the rate of interest or of the amount of the free balance to be maintained by the depositor. It may be possible to induce the depositor to increase his average balance or make a more equitable distribution of out-of-town items as between his several bank accounts.

It is my belief that most people want to be just in their business relations with their fellowmen. If, as a result of a cost system worked out with some care, taking into consideration the size of the institution involved, it develops that an account can be shown to be on an unprofitable basis, a frank disclosure of the facts by the bank will result in some equitable arrangement to correct the condition.

In this discussion with the depositor, the banker must start off with a few clearly demonstrable facts before he launches into such abstract and debatable factors as the cost of handling an item or the overhead applicable. In many cases he will not reach those two factors before he has convinced his man that an adjustment is necessary. It should not be difficult to show that it costs something to lend money at 6% so that the actual rate earned is below that figure. There will be a little trouble in convincing him that instead of a daily average balance of $2,750, as shown by his books, the bank really had available for investment only $1,000. That will be difficult, but if the banker is a good salesman and knows his business he ought to be able to prove his case. The matter of the cash reserve and the interest paid the depositor on his account are simple facts.

I am also of the opinion that any sum of money within reasonable limits expended for the installation and maintenance of a cost-analysis department suited to the requirements of the particular bank will be a worth-while expenditure and produce dividends for the bank. It would, of course, be ridiculous to expect a small country bank to adopt a cost system in the same detail as would be desirable in the large city bank. However, a system based upon certain fundamentals can be devised to fit both the large and the small bank. The only difference need be the degree of fineness or extent to which the analysis shall be carried.

Such a system would appear to have been devised by the federal reserve bank of New York under the title *Analysis of Depositors' Accounts—Short Method.* Numerous other systems have been studied, but for simplicity and general practicability, this scheme appears well adapted to the needs.

Inasmuch as "activity" is the principal factor of cost, it follows that the bulk of the expense applicable to a depositor's account will be allocated to the account on the basis of the number of items deposited and charged. It is also fundamental that amounts in transit should be eliminated from the daily basis before crediting the account with its proportion of the income from loans and investments.

If the bank desires greater accuracy in its costs, it would do well to heed the advice in this federal reserve pamphlet with regard to subdivision of the items into classes such as city, clearing house, country, etc., for the purpose of ascertaining the cost of the various kinds of items. It will be obvious that an out-of-town item will cost more to handle than a clearing-house or city item.

The apportionment of expenses on an equitable basis to the various departments undoubtedly presents the most difficult problem. However, a little care in this respect should result in a segregation as between expenses applicable to deposits and expenses not so applicable. For instance, no part of the expenses of safe-deposit, trust or foreign departments should be used in determining cost of depositors' accounts. Another point to bear in mind is that certain expenses will form a primary group and others a secondary group. The result, after deduction of the first group, may be termed gross profit and, after the second group, net profit.

In any cost system there will be found a group of expenses known as overhead or burden, spread over the cost of the article manufactured on the basis of direct labor, material consumed, or perhaps both combined. This plan also provides for such a group spread partly on the basis of the number of deposit accounts and partly on the basis of size of deposit. Perhaps size is the least justifiable base and any large apportionment in that class should be discouraged.

In conclusion it would appear that some method of cost analysis is as essential for the banker as for the manufacturer or merchant; that the general adoption of the scheme is dependent upon an educational process which bankers themselves must conduct; that the benefits both to banks and the public, generally, will be well worth the effort expended; and that there is now in this federal-reserve plan a workable system which can be expanded or even contracted to fit each particular situation.

Importance of Accounting to Management *

By A. R. Erskine

While we can look back to the ancients for the beginnings of accounting, it was not until recent times that modern accounting as we know it was devised. Until the advent of the machinery age, transactions of buying and selling and exchange of money were adequately served by the simplest of systems. When big factories with mechanical appliances, employing numerous men, began displacing hand-work, the industrial era started, and accounting became complex. The rapid multiplication of such industries increased the problems and it soon became apparent that manufacturing accounting was the most difficult task that had yet faced the accounting fraternity. The subject was most baffling. The old merchandise account was continued, to which goods made or purchased were charged at cost, and sales were credited at selling prices. Costs of product were estimated by crude methods and inventories were priced at these costs. Inventory periods were dreaded because of the difficulties of pricing, closing down and making up balance-sheets and trading accounts. Balance-sheets and profit-and-loss statements in the comprehensive and intelligent form of the present day were unknown. Audited and certified statements such as are now commonly required were likewise unknown; and it is safe to say, perhaps, that statements really correct were seldom obtained. Manufacturers naturally sought men skilled in accounting practice to help them out and while such men knew more than the bookkeepers employed by the manufacturers, they had only a scant knowledge of modern accounting as we know it today. These accountants, however, enjoyed a lucrative practice, formed a profession and studied hard.

As the first great modern industrial country, it was natural that England should first appreciate the importance of accounting and dignify men engaged in it publicly by state recognition. England has the distinction of first creating by law the chartered accountant, about two generations ago, and of establishing accounting on a high professional plane approaching that of law. Professional accountants were meantime practising in the United

* An address before the Illinois Manufacturers' Association, Chicago, 1924.

States and in 1896 they succeeded in having the legislature of the "empire state" pass a law recognizing the profession, under which the board of regents examines applicants and grants C. P. A. certificates to successful candidates. All our forty-eight states now have C. P. A. laws. All examinations include commercial law subjects as well as accounting.

It was about 1896 that our big industries began forming, and the certified public accountants of the country have performed highly efficient and comprehensive work in the installation of new systems, improvement of existing systems, standardization of balance-sheets, profit-and-loss statements, auditing methods, etc. Big business could not have prospered as it has without the aid of these men and it cannot get along without them today. Our federal government has used them in the formation of laws and accounting systems with the interstate commerce commission, the internal-revenue department and many others. They have performed invaluable services for our railroads, mercantile and financial institutions and thousands of income-tax payers depend upon them to make out their returns. Bankers, stockholders and investors demand their certification of corporation balance-sheets, profit-and-loss statements and prospectuses.

In defining the word "profession," Webster says: "the three professions, or learned professions, are especially theology, law and medicine." He includes neither chemistry, engineering nor accounting, which are so important to the conduct of business. Theology and medicine give their greatest expression outside of business and in our home life, but law, chemistry, engineering and accounting subsist on business and are a part of it. Professional accountants play their part, as has been said, but vocational accountants employed by industry are responsible for results in individual institutions.

The comptroller or general auditor of a corporation should be an expert accountant. He should know the theory and practice of general accounting as well as the professional accountant and infinitely more about the problems of his own concern. He is the diagnostician of the business. His bump of curiosity is of abnormal development and he takes nothing for granted. He knows what is going on. He is resourceful, courageous, aggressive and determined to get the facts and disclose them to the management. Although he is a bold man, he must be tactful in order to keep the friendship and get the coöperation of the organization. No man is stronger than the organization, and tactful men realize this. The best comptroller is one who calls the attention of the management orally, or by special letter, when it fails to act in a dangerous situation.

The treasurer of a big corporation should be an expert accountant and have the courage of a lion. The real treasurer, as I comprehend him, is the man unafraid, when danger threatens, to say "no" to his president or his directors when occasion demands and to show him or them why. He should be prepared to accept dismissal rather than to permit grave risks to be taken. If the treasurers of all the corporations of America during 1919 and 1920 had been this type of man, most of the inflation and huge losses of business would have been avoided. We all know of several presidents who ran their corporations in debt during this period without realizing the significance of their actions at the time. This fact is one of the best evidences of the importance of accounting to management.

The responsibility rests on the comptroller in coöperation with the treasurer of every corporation for the character of its accounting system, for therein lies the secret of success. Some systems are almost choked to death with red tape. They anger the production and sales departments, puzzle the accounting forces, cost a barrel of money and are Greek to the management. Capable comptrollers will not permit such systems to endure. To be of real value, accounting systems must be comprehensive, simple and economical. They must not clutter up the factory with time tickets, material tickets and other minutiæ. Departmental records must be kept only as the basis for operating reports that are actually required by the management. When the cost of keeping records and making reports exceeds the loss that might be sustained without them, they become inadvisable.

Big business generally is equipped with efficient accounting systems which comprise, in brief: (1) original records kept in different departments showing receipt and disbursement of money; purchasing, stocking and use of materials and supplies for production, construction and equipment; the movement of finished goods; and collection and payment of accounts; (2) operating reports made from these records for the information of the management; and (3) financial reports for the information of management, directors and stockholders. These reports, made daily, weekly and monthly, show what has happened in the business. Unless management thoroughly understands them, however, and uses them to correct wrong conditions and take further advantage of opportunities which they disclose, their value is diminished. The management should possess at least a good working knowledge of accounting. The possession of even brilliant talent for manufacturing or selling or both is not enough. There are many details of big business which management must watch vigilantly. Plant equipment and methods of manufacture may be economical and proper or otherwise. The number of employees, salary and wage-rolls, kinds and cost of materials, costs and prices of product, markets and sales efforts, financial condition and profits, are always live questions. Reports from the accounting department disclose the facts concerning them all. Every member of the management from the foreman up to the president should be an analyzer of reports and a seeker after improvements. These things illustrate the importance of accounting to management. They show why it is impossible to conduct a business intelligently and successfully without an adequate accounting system. While such systems generally prevail in big corporations, many smaller concerns are wofully lacking in accounting facilities. Such concerns will bond their cashier to prevent him from stealing the cash in the bank or the cash drawer, and maintain no checks whatever on their inventories or receivables, which usually represent three-fourths or more of their total assets. On the theory that a dollar saved is a dollar made, they spend money reluctantly. They think only of accounts and never in percentages. When sales can be increased by an increase in the amount of expenses without increasing the expense ratio, they seldom grasp the opportunity. When new machinery or new methods will justify the scrapping of old equipment, they may never comprehend it. Modern accounting methods are adaptable to such concerns, whether they be engaged in manufacturing, jobbing or retailing, and will pay their cost if operating reports are properly utilized by the management. It is my conviction that efficient accounting systems applied to business generally in the United States and used intelligently by management would save scores of millions of dollars annually.

In conclusion, I would like to make brief reference to the present state of business. Our production, transportation and distribution activities are the source of our wealth, employment, wages and happiness. I always like to define business as "organized society working to produce and distribute the things it needs." If this definition be accepted, then obviously any interference with society in its activity is an injury to everybody in the country. It is awfully easy to disturb business by undermining confidence. When this is done, unemployment ensues, with the misery it entails. The country has been flooded with bearish propaganda deliberately intended to undermine confidence, frighten security holders and hurt the business of the country. It was and is distinctly and deliberately hostile to the business of the country, to the prosperity of the nation and to the happiness of our people. A prominent financial magazine has described the cumulative effect of bear raids on the stock market. It says:

> "As pressure is put upon the stock market, there is less optimism, then more pessimism, then loss of confidence, decreased buying power, reduction of gross business with consequent increase in overhead, which means lower net earnings. These factors in turn frequently force reductions in dividends, and this has an even more depressing effect upon stock prices. It is a vicious process. Short selling does not destroy confidence, but raiding the market does, particularly when it is accomplished by propaganda originated by and intended to aid bear operators. The bear may claim that it is just as illegitimate to boost stocks unduly, but a creation of artificial values on the bull side does not have such a detrimental effect in the way of injury to business and creation of unemployment."

Business is frequently assailed and sometimes penalized because it is big, whereas the truth is that our big industries are the very ones that have made our country what it is. Big business is the difference between the United States and the rest of the world. America was not industrially great with its small industries of thirty years ago. I remember when industrial workers were making from ten to twenty cents an hour, when a few owned their homes, and men who owned bicycles were considered fortunate. Big business has made it possible for workers to own modern homes, automobiles, talking machines and radios. Big business has made necessities out of luxuries by mass production, which put them within the reach of the average man. Big business has advanced the living standard of America to a high level hitherto unknown in history. It has converted America into the world's greatest industrial nation and made our big cities what they are. All great modern nations have been industrial nations, and industry is the life blood of this nation. Big business, lawfully conducted, is the greatest asset of the nation. Every governmental agency and the power of the people should always be exerted towards its maintenance and prosperity.

The Training of Accountants in England*

By T. H. Sanders

Accountants' Societies

There are two societies of public accountants in England, the Institute of Chartered Accountants in England and Wales, and the Society of Incorporated Accountants and Auditors. The former was founded in 1870 and was incorporated by royal charter in May, 1880; this later date is therefore commonly used as the date of its inception. The Society of Incorporated Accountants and Auditors was established about 1885 by a group of men who were for various reasons ineligible for membership in the Institute of Chartered Accountants or were dissatisfied with the rules of admission to the older society. But as soon as this newer society had established itself and obtained public recognition, it proceeded to set up standards of conduct and requirements for candidates for admission which were substantially the same as those of the older institute. At the present time it is probably fair to say that the Institute of Chartered Accountants is the ranking association and has the greater prestige; but there is no substantial difference between the two societies in their rules, conditions for membership and severity of examinations. The Institute of Chartered Accountants had a total membership of 5800 members on September 1, 1922, and the Society of Incorporated Accountants and Auditors had a membership of 3600 on December 31, 1922.

Legal Position of Accountants

The status accorded to public accountants in England by legislation has so much to do with their training and general practice that the picture would not be complete if I did not quote to you certain passages from statutory enactments bearing on the subject.

The companies (consolidation) act of 1908 is an assembly, in one statute, of previous legislation and court decisions relating

*A paper read before the Ohio certified public accountants, Ohio State University, Columbus Ohio, 1924.

to business corporations. Among others, it contains the following provisions:

> 112. (1) Every company shall at each annual general meeting appoint an auditor or auditors to hold office until the next annual general meeting.
> (2) If an appointment of auditors is not made at an annual general meeting, the board of trade may, on the application of any member of the company, appoint an auditor of the company for the current year, and fix the remuneration to be paid to him by the company for his services.
> (3) A director or officer of the company shall not be capable of being appointed auditor of the company.
> 113. (1) Every auditor of a company shall have a right of access at all times to the books and accounts and vouchers of the company, and shall be entitled to require from the directors and officers of the company such information and explanation as may be necessary for the performance of the duties of the auditors.
> (2) The auditors shall make a report to the shareholders on the accounts examined by them, and on every balance-sheet laid before the company in general meeting during their tenure of office, and the report shall state—
> (a) Whether or not they have obtained all the information and explanations they have required; and
> (b) Whether, in their opinion, the balance-sheet referred to in the report is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs according to the best of their information and the explanations given to them, and as shown by the books of the company.

This act does not expressly specify who may act as auditors: there is no requirement that he must be a member of one of the two societies. But it is a fairly common thing for acts of parliament which call for accounting and auditing work to be done, to specify that only a member of the Institute of Chartered Accountants or of the Society of Incorporated Accountants may do it. This is true of the act of 1903 relating to the audit of municipal and other local government authorities.

Since all accounting activities in England turn about these two societies and since they are for present purposes so very similar in their procedure, it will give a sufficient picture of English conditions if I describe how a young man may become a member of the Institute of Chartered Accountants.

Requirements for Admission

In order to qualify for membership in the institute it is necessary for a man to serve an apprenticeship of five years in a public accountant's office; the contract in which the apprentice is employed is commonly referred to as the "articles" and the young man is an "articled clerk." He is also required to pass three examinations; a preliminary examination which will be taken prior to the article being signed, an intermediate examination to be taken after half the term of apprenticeship has expired but before its completion, and the final examination to be taken after the period of apprenticeship has been completed. In case it should be thought that the institute is not strictly up to date in some respects, it may be stated that the dates of the examinations for the year 1930 have already been fixed as November 25 to 28, inclusive.

Articles of Clerkship

Articles of clerkship cannot be signed until the candidate has passed the age of sixteen and has passed the preliminary examination. One of the by-laws of the institute specifies that a member may not have more than two articled clerks at one time. The articles specify in general that the clerk shall work in the offices of his principal and shall be afforded facilities for acquiring knowledge and experience in accounting. The clerk is prohibited from taking on any other occupation during the period of his service, and there are a variety of technical rules relating to the legal aspects of the contract itself. It is more important for us to observe that a premium is commonly paid by the clerk to his principal, ranging from 100 to 500 pounds sterling according to the standing of the house which is granting the articles. This circumstance practically limits the profession to those boys whose parents are in a position to put down this sum of money.

The Society of Incorporated Accountants and Auditors differs from the institute in that it does permit men to apply for membership, without having served an articled apprenticeship, if they can present a certificate from employers that they have served in the profession for nine continuous years and have passed the required examinations. This means that the profession is not absolutely closed to men who do not wish to serve a five years' apprenticeship, but the opening is an exceedingly slender one. It depends upon the willingness of a member of the profession to employ a young man without articles and without a premium, and that condition is rarely found. While it is true, therefore, that technically there is another way into the profession, for all practical purposes the apprenticeship is the almost universal entrance.

Preliminary Examination

As one would expect from the fact of its being taken prior to the signing of articles, the preliminary examination is general in character. The compulsory subjects include English dictation and composition, arithmetic, algebra and geometry, geography and history. For optional subjects candidates must choose two from the following: Latin, Greek, French, German, Spanish, and Italian; advanced mathematics, physics, chemistry, geology and stenography. The range of knowledge required within these subjects would necessitate that a candidate for this examination should have attended a secondary school of good standing. The examination, itself, may be waived by any candidate who presents evidence of equivalent achievement. There are several well-known public examinations which are accepted for this purpose.

Intermediate Examination

As already stated a clerk must have completed at least half the period of service before he can present himself for intermediate examination. The examination consists of four papers of three hours each: the first covers general commercial knowledge, including the principles and uses of bookkeeping; the second is upon bookkeeping and accounts, with special reference to corporation accounting; the third is also upon bookkeeping accounts, but with special reference to partnership and executorship accounts; and the fourth relates to auditing of various classes of accounts, with a proviso that "the syllabus does not necessarily exclude the setting of questions in kindred subjects, such as costing and taxation." It will be seen that a considerable range of accounting and business knowledge is already required of the young man, and the mortality in this examination is considerable, ranging around 30%.

Final Examination

For the final examination the following subjects are required: two papers in advanced bookkeeping and accountancy, including costing and taxation, and the headings to this general title would suggest that there is not much in the accounting field which may not be called for under this heading.

Auditing, including all classes of accounts.

Partnership and executorship law and accounts, including the right and duties of executors, trustees and receivers.

Bankruptcy and company law.

The principles of mercantile law and the law of arbitrations and awards.

The candidate must also offer two of the following three subjects: economics, banking, currency and foreign exchanges, actuarial science. This examination also is of considerable severity and usually about 40% of the candidates fail in it.

Practical Training of the Articled Clerk

While there is very little positive guarantee that an articled clerk will really get an opportunity to practise accounting and come in contact with various types of business, yet it usually happens that any articled clerk who shows diligence and industry is afforded full opportunities to acquire the necessary experience. During the first year he is little more than an office boy, doing such odd jobs as filing, running errands, press-copying. He is then given various bookkeeping tasks which will progress in difficulty in proportion as he shows aptitude for handling them.

The English practice still continues of making detailed audits in which every little posting and footing is checked, including all personal accounts. This provides an inexhaustible field for keeping young clerks busy. American accountants always wonder very much at this circumstance; but it is fair to say that English accountants and manufacturers wonder just as much at the elaborate and detailed records of cost of labor and materials which are kept in many American factories. I will not attempt any explanation of these phenomena, but content myself with indicating that the astonishment is mutual. In England it is also quite common for public accountants to keep the books or part of the books of various firms. This provides plenty of opportunity for young clerks to acquire their early experience. Under the legal provisions already cited, public accountants play a very important part at company shareholders' meetings. The law places considerable powers in the hands of the auditors, making them the representatives of the stockholders, so that they appear at company meetings and present their report publicly to the stockholders. Also the accountants frequently write up the minutes of the corporation. It is a great convenience to the principals of the firm in the execution of these duties if they can take a young clerk along with them as private secretary and general assistant. In this way the articled clerk will have considerable opportunity to come in contact with business men and business affairs and to understand the uses of accounts in relation thereto. A young man who shows industry and ability will in this way be able to commend himself to his principal, who in turn frequently acquires a considerable personal interest in and affection for his young protegé, in addition to the business relationships.

It is easy to see that a young accountant's success or failure will be largely influenced by the extent to which he takes advantage of the opportunities thus afforded him. If he is disposed to be negligent and good-for-nothing, he will be afforded every opportunity to follow his disposition and probably nobody will consider it his business to worry about him.

Student Societies

In all the large towns there are local societies of accounting students which, although they are not included within the official activities of the Institute of Chartered Accountants or of the Society of Incorporated Accountants, are nevertheless very closely associated with the parent societies. The accountants in the district will usually organize the students' society, draft its constitution, provide officers from among their own members, and give financial aid to the provision of a library and other services of benefit to the young accountant. The Chartered Accountant Students' Society of London has 1400 members at present, and their president is Sir William Plender, a former president of the Institute of Chartered Accountants. They hold weekly meetings at which they hear lectures from leaders in the accounting profession; they organize joint debates with other students' societies; they have short papers presented by their own members and open discussions on a variety of subjects, frequently covering the questions set in the last examinations. They also organize special coaching classes for the examinations. These students' societies are a very important factor in the development of accountants in England, not only for the aid they give to the individual student in learning the subject matter of accounting, but also for the strong professional sentiment and esprit de corps which is developed among them. There is no doubt that these students' societies have in this way contributed largely to the importance and dignity which the accounting profession has assumed in England.

Training for Examinations

In spite of the activities of the students' societies articled clerks are left very largely to their own resources in the matter of getting through the examinations. For this purpose they will usually join a coaching class; if there is one connected with their local students' societies they will usually join it; otherwise they are likely to take a correspondence course with some firm which has specialized in accounting examinations. A few years ago one of these coaching houses regularly coached about 75% of all the candidates who were submitting themselves for the examination for the Institute of Chartered Accountants. The students' societies are coming more and more to develop their coaching activities, but private coaching establishments nevertheless continue to flourish.

Character of the Examinations

It will readily be understood that, with all phases of accounting dominated in this way by the members of the profession organized in the two parent societies and the affiliated students' societies, the instruction in the subject and the examination questions themselves take on an extremely practical aspect. The examination papers are a direct reflection of the practical activities of the practising accountants who write them. There is a notable absence of many of the theory questions with which we are familiar in this country.

The Place of the Universities

A university graduate is allowed to curtail his term of apprenticeship from five to three years and is, of course, exempted from the preliminary examination. Professors of accounting in universities are usually selected from the ranks of practising accountants and are frequently given an honorary degree of the university in order that they may wear a master's gown at lectures, and thus look like the other professors. There is in England no large body of men like the American Association of University Instructors in Accounting, nor are there the hundreds of universities and colleges with commercial departments that we have in this country. The first faculty of commerce in England was established in the university of Birmingham in 1902. I entered as a student at that time, our professor of accounting being Lawrence R. Dicksee, who came down in the London express and a silk hat one day every week. The character of our instruction will be evident to all who are familiar with Dicksee's books.

It is my impression that the development of accounting in this country as an academic subject has had considerable advantages in the development of less technical text-books and in teaching methods which are better pedagogy than is ordinarily practised in England. The subject is in this way unfolded to the student in an orderly, logical manner, and much is done to make the subject matter easily acquired. So much of the instruction in England is prepared for the articled clerks who are in daily contact with practical accounting that a good deal is left to the imagination. A student who receives his instruction entirely within an English university is, therefore, at some disadvantage, and it is my recollection that I found it somewhat hard going to follow Dicksee's lectures, which he always read from typewritten manuscripts.

It is fair to say that it is possible to go too far in the direction of making accounting easy, and perhaps one of the reasons why public accountants in America have occasion sometimes to be dissatisfied with the product of our colleges is that said product has been carried along by a system of "spoon-feeding," of accounting made easy, when he had no particular aptitude for it. In England it is more a case of the survival of the fit, and any man who does not have considerable liking for the subject or considerable ability in it will probably not survive the strenuous regime which is set up for the man who wishes to become a public accountant.

Remuneration

It has been stated that the articled clerk pays for the privilege of working for five years in his principal's office. Sometimes the premium is returned to the clerk, in instalments spread over the last three years of his term. This, however, is entirely optional with the firm. If it thinks itself a very superior house, it will consider that the young man is very fortunate indeed to see the inside of the organization, and the premium will not be returned in any way. It follows from this, that if a man pays a premium of 100 pounds for his articles, he is likely to get it back; but if he pays 500 pounds, it is probably gone for good.

After he has completed his articles and passed his final examination, the clerk can as a rule get only a very modest remuneration indeed by staying with the same firm; and probably could do very little better by going to any other. There are always considerable numbers of men in the market who have reached this stage, and who, for various reasons, are not yet ready to start firms of their own. Even with considerable experience, therefore, the compensation paid to qualified clerks in accountants' offices would look very meager to Americans. It is at this stage that many of them come to this country. But there is, of course, in England, a steady demand for men who have completed their training to serve as senior clerks. The remuneration for this class ranges from 250 pounds to 500 pounds, say from $1,200 to $2,400. One also finds in England the same movement as is observable in this country, of men leaving the profession to enter industrial concerns.

Classes of Members

Having completed the articles and having passed the final examination, a man is entitled to membership in the institute as an associate member, in which capacity he may use the letters A. C. A., associate chartered accountant. An associate is a full member in every sense of the word, but when he has been in practice five years continuously he may apply for a fellowship in the institute, in which capacity he may sign himself F. C. A. The fellows are the seniors in the institute and the most prominent members of the accounting profession in England.

It is still provided in the rules of the institute that there is one method of getting into the institute other than by serving the articles and passing the examinations. If a man "can prove continuous connection with public accountancy from date before the incorporation of the Institute (11th of May, 1880)," he is entitled to membership.

Scope of Public Accountants' Work

It has already been mentioned that the law requiring that company accounts shall be audited by public accountants and a report made direct to the stockholders puts a considerable amount of authority in the hands of public accountants in England. Every year the company's auditors are reëlected publicly at the stockholders' meeting. It is true, of course, that a majority of the stockholders can elect any auditor they choose; nevertheless, they could not very well recommend a change of auditors without giving satisfactory explanation for so doing; and some of the stockholders present would be likely to ask the auditors for their version of the affair.

In this country much has been made recently of the fact that it is the common thing for accountants in England to act as receivers, arbitrators, liquidators and in similar capacity, and it is argued that American accountants should be afforded similar opportunities. There is no doubt that there are in America very many accountants who would be fully qualified to act in this sort of capacity. It is fair to point out, however, that a good deal of attention is paid to these subjects in the training of English accountants, as is evidenced by the considerable place they occupy in the examination papers. A man cannot come to be an accountant in full standing in England without having been very well trained in the law and practice of receivership, bankruptcy and arbitration; and it is not unreasonable to suppose that a wider acquaintance with these matters will be a prerequisite to any considerable extension of the operations of American accountants in this field.

Conclusions

Professor Eckelberry invited me to draw some conclusions as to the relative merits of the American and English systems. That is a rather dangerous enterprise, and I must admit that some of the comparisons which I have previously seen do not fill me with confidence. Happily the comparison is largely unnecessary: in each country the practices in vogue are an adaptation to their own circumstances, and are probably the better practices in those circumstances. It is commonly held that the labor market and public sentiment are such in America that the English apprenticeship system could not be introduced. Certainly it could not be introduced at present in its entirety, but I am not altogether sure that parts of it will not appear in this country at some future date. We speak of the payment of an apprenticeship premium as a curiosity: but thousands of young men in this country are paying equal sums to get courses in universities or from correspondence schools. Is it not possible that some day some of these young men might come to the conclusion that it would be just as good an investment to put their time and money into training within a public accountants' organization? Even if they are not willing to pay a premium—and I hardly expect that—might not some of them be willing to serve for a term without remuneration, during which time they might learn what they could in the offices of their employer and his clients? Some of the larger accounting offices in the east are now giving systematic instruction within their own firms and remuneration tends in some cases to be lower during this training period, than the normal going market rates.

I have just been privileged to see a paper which my colleague, Professor J. Hugh Jackson, read last Saturday before the American Institute regional meeting at Pittsburgh. Professor Jackson dwelt on the shortcomings of the young men who offer themselves as juniors to our accounting firms, and how some of these shortcomings are being met by the courses of instruction given within the accounting firms. Is it not possible that, if internal organized instruction of this sort becomes common, it may grow into a sort of compromise between the present American system of just hiring junior clerks and the English apprenticeship system? To be specific, I do not expect to see American youths paying large premiums to be bound apprentices for five years: but I do think it possible that American accounting firms may develop a satisfactory form of abbreviated and intensive apprenticeship which may so appeal to our young men as a good opportunity for advancement that they will be willing to serve a short period at it either with no pay at all or with very little. If accounting firms are willing to employ competently trained instructors—and several of them have already employed some of the ablest instructors in the country—then this form of professional training might result in a happy combination of the American and English systems.

As to the type and quality of accountant produced respectively by the two systems, I would wish to speak very guardedly. Many excellent accountants have been trained in each country. In the paper previously referred to, Professor Jackson regretted, among other things, the young American's lack of ability to express himself well in English, to be thorough, systematic and clear in his thinking. If I may say so, much of this originates, not in our universities, but in our primary and secondary schools. If a man is to be taught to think straight and speak clearly, the surest way is to catch him young. I am disposed to think that the fundamentals of English grammar, composition and arithmetic are drilled into English school-boys somewhat more thoroughly than is done here: though in saying this I am fully aware of other things which the American schools do better. When there is superimposed upon this early English school training the necessarily exact and careful work of the professional accountant's office during a five-year apprenticeship, it is to be expected that, on the average, the resultant product will be better trained in technique, in the exact and efficient handling of routine work, in all that goes to make a good junior.

But, it is sometimes argued, the value of the training ends there—the apprenticeship system produces patient plodders who can check and add to perfection, but they lack breadth of view, constructive ability, adaptability to the multiplicity of business situations and practices. The detailed audit of England, with its minute checking of accounts, is often cited to prove the case. In spite of the evidence, however, I doubt the conclusion, as a general thing. I have already mentioned that, in addition to helping with detailed checkings, the young English clerk frequently accompanies his chief to company meetings and hears him there present the annual report. He will be in close touch with many important business transactions and conferences which will tend to dispel any idea in his mind that the figures and verifications are the ultimate end. As he advances through the various stages of the profession, he will himself participate in these business discussions. It is a mistake to imagine that the detailed checking and the mechanical work is all they do. These things must be taken in conjunction with the legal provisions making the auditors the representatives of the stockholders in the councils of the business. I was private secretary to the president of a large manufacturing concern and worked in his private office. There I frequently heard the discussions which took place between the executives of the business and the auditors, and it is a simple fact that the latter were a very real influence, not only in determining the form and content of annual statements, but also in all the major policies of the company.

Of course, all American accountants worthy of the name do the same thing. In defending the English accountant on this particular point I do not intend to say he has any advantage, so far as his ability and training are concerned, over his American brother. But just to complete this line of argument, it is worth while to point out the greater extent to which English accountants enter public life. Several of them are members of parliament; accountants have been lord mayors of cities like London and Birmingham; and they are conspicuous in many other public activities. One may also point to the large numbers of men trained in

England or Scotland, who have become principals in leading American firms.

It is probably true, however, that American audits and investigations accomplish more, in proportion to the time and effort put into them, than do English audits, by reason of the elimination of the detailed checking and concentration upon the broad features of the case. The balance-sheet audit has been developed into a much more effective instrument for establishing the status of a business in America than in England. The conditions of business life are more varied in this country and American accountants have therefore developed an adaptability to and resourcefulness in these conditions which it would take the English accountant a little time to acquire. But here again the reverse is true, and there are conditions in England which at first would puzzle American accountants.

Lest these remarks should appear confused and contradictory, allow me to summarize in a few words. I think there is no doubt that the English apprenticeship system produces better junior technique and thoroughness, though the young Americans, especially the college trained, will have a better background and all round experience. Beyond this point there is in both countries that weeding-out process which results in the survival of the fit; and the fit in both countries look very much alike. Forms of business organization and administration have grown up in America which have encouraged among accountants a greater freedom in the processes by which they establish the status of a business. But the differences in this direction are less than those people suppose who concentrate their attention upon the English practice of detailed checking.

The JOURNAL *of* ACCOUNTANCY

Official Organ of the AMERICAN INSTITUTE OF ACCOUNTANTS

A. P. RICHARDSON, *Editor*

EDITORIAL

St. Louis, 1904–1924

In the pleasant and central city of St. Louis there will assemble on September 16th members of the American Institute of Accountants and guests from various foreign societies for the annual meeting of the Institute. There has been a great deal of captious criticism of the climate of St. Louis in September. Some commentators have expressed the opinion that St. Louis is the hottest place in the United States. This, however, is slander, and it is particularly unmerited slander when applied to that portion of St. Louis in which stands the hotel that is to be the meeting place. By the middle of September there is every reason to expect cool and refreshing breezes in the Mississippi valley. It may not be necessary to bring heavy overcoats and furs, but there will be comfort, and in addition there will be welcome as warm as the climate is unjustly reputed to be. This will be an exceptionally important meeting inasmuch as it is the twentieth anniversary of the congress of accountants held at the time of the St. Louis World's Fair, the congress out of which grew the American Association of Public Accountants in its later form and subsequently the American Institute of Accountants. The committee on arrangements is making a special effort to insure the attendance of all the veterans who were present in 1904, and it is hoped and expected that there will be delegates from nearly all the foreign societies which were represented on the earlier occasion. The committee expresses the wish that there may be present not only the members of the Institute, but also all other persons who are interested in the practice of professional accountancy. There will be room for all at the open sessions which will be held on the 16th and 17th days of the month. Those who expect to find it convenient to attend may obtain detailed information from David L. Grey, chairman of the committee, 506 Olive Street, St. Louis, Missouri.

Retrospect and Prospect

Some day an accountant-historian will sit down and prepare for the benefit of those coming after him an outline of the various forward steps that have been taken by practitioners in this country. He will record the first public recognition of accountancy as a profession as an event of not many years ago. He will note the laws enacted by the states providing for the issuance of certificates to accountants who meet a certain standard of proficiency and trustworthiness. He will chronicle the ever-widening field of service of accountancy. He will show that accountants have been keeping step in the march of business with its ever-increasing intricacies. He will set forth in detail the nature of the new duties thrust upon public accountants in the conduct of business of city, state and nation. He will describe the duties which should be performed professionally and those which are in the nature of public service for which the accountant, by virtue of his knowledge, is most fitly adapted. He will record with a sense of gratification how the accountant is being more and more sought to assist in the making of public policy, in the presentation of facts, in the betterment of the whole business world. The twenty years which have elapsed since that memorable meeting of public accountants in St. Louis constitute a period so fruitful in development and so rapid in progress that our historian may be forgiven if he ventures into the realm of the superlative when he makes prediction for the next twenty years. No limit may be set to the possibilities before us.

New C. P. A. Bill in Louisiana

Both houses of the legislature of Louisiana have passed a bill providing for amendment of the C. P. A. law of that state. The full text of the bill appeared in the bulletin of the American Institute of Accountants published July 15th. The new law is an improvement, chiefly because it follows the trend of legislation toward the restriction of the practice of professional accountancy. The language of the bill is in many respects similar to that of the Maryland law. Practice is to be confined to those who are registered by the board of certified public accountants of Louisiana and to those who may be in practise at a given date. The latter class will hereafter be known as "public accountants." All others entitled to practise must be certified public accountants so licensed by the state board of accountancy. The public-accountant class under this bill is therefore a disappearing body, inasmuch as there can be no accessions to it and those entitled to classification in it will pass out of accounting, seek to obtain recognition as certified public accountants or in the course of time be removed from the field of practical politics. The history of legislation in Louisiana is somewhat checkered. The original law there provided so generously for the issuance of waiver certificates that a great number of persons received certificates who could by only the greatest stretch of imagination be considered accountants. The law, however, has been well administered of late years, and the examinations have been conducted in coöperation with the American Institute of Accountants. Now the accountants in Louisiana feel that the time has come to limit the practice of the profession to those who are licensed by the state, and we have, therefore, the new bill, which has received the signature of the governor. Louisiana, therefore, takes rank as the second state in the union to have absolutely restrictive legislation, unless with Maryland we include Oklahoma, which has had a rather anomalous restrictive law on its statute books for some time.

Legislative Clouds on the Horizon

Speaking at the regional meeting of the American Institute of Accountants held at Wilmington, Delaware, June 26th, Raymond C. Reik, Maryland, presented an able and interesting review of the developments in accountancy legislation with special reference to the Maryland statute. This matter has been the subject of discussion in THE JOURNAL OF ACCOUNTANCY in recent issues, and it is therefore unnecessary to present all of Mr. Reik's remarks. In the course of his address, however, Mr. Reik made a statement which was exceptionally impressive. He said, "During the year 1925, forty-seven legislative assemblies meet in the United States or its territories, in fact in all except Kentucky, Louisiana, Maryland, Mississippi and Virginia." It is an unusual combination of circumstances which will bring about so much legislative activity. The statute books of our long-suffering country will be burdened more heavily than ever before, and an infinite number of perfectly useless laws will be enacted. Out of the great mass of legislative nonsense which will result, it is hoped that there may be a modicum of really valuable legislation, and one of the directions in which vital developments may be expected is that leading toward better regulation of the profession of accountancy. The forty-eight states of the union, the District of Columbia, Alaska, Hawaii and the Philippine Islands have C. P. A. laws. Of the five states whose legislatures do not meet next year, two, namely Maryland and Louisiana, have enacted restrictive legislation. With the exception, therefore, of Kentucky, Mississippi and Virginia, there will be an opportunity for the betterment of accounting control in all parts of the United States and its territories during the coming year.

Investigating the Trend of Opinion

The accounting profession is not a unit in its commendation of the principle of restrictive legislation. Many deep thinkers among the practitioners of the profession feel that the time has not come for limitation of the practice of accountancy; but there will probably be no difference of opinion among reputable practitioners everywhere as to the desirability of making more effective the regulations governing that portion of the profession which is entitled to the designation "certified public accountant." Most of the state and territorial laws are founded upon a form of bill prepared originally by the American Association of Public Accountants and later somewhat amended and adopted by the American Institute of Accountants. There is hardly a law in the land which has not been directly influenced by this model bill. The committee on state legislation of the Institute feels now that the time may have come to embody certain amendments in the model bill, keeping pace with what seems to be a more or less wide-spread tendency toward the enactment of restrictive legislation. Members of state boards of accountancy, and many members of the Institute as well, have been asked by the committee to present comments upon the bill as it stands and suggestions for amendments which may seem desirable. This is a subject of national interest, and it is hoped that the committee, as a result of its investigations, may be able to present suggestions for the consideration of the council which will represent the best thought of accountants everywhere.

Statutory Language and English

While on the subject of state laws, it may be permissible to express a fervent hope that some day there will appear on the statute books of one of our states a law written in English.

This simple wish is expressed, not in any spirit of contentious criticism. It is uttered more in sorrow than in anger. But the fact remains that most of the laws produced by our extremely fecund legislatures come to birth in a form which reflects no credit upon their parents. There are probably many excellently worded bills introduced by legislators, but by the time trifling amendments are made, clauses are substituted and punctuation gaily scattered, the result becomes almost unintelligible at the worst and, at the best, atrociously ungrammatical. There is now before us one of the recently enacted C. P. A. laws which would break the heart of any high-school student who was requested to parse it. It simply wouldn't parse. It is not to be expected that every legislator will be a purist in English, but surely it is not asking much of the law makers that they employ someone who knows English to review legislation before it is printed. Perhaps this suggestion will be favorably considered when it is borne in mind that it would make a job for some worthy constituent.

In Search of a Word

The committee on terminology of the American Institute of Accountants has not given consideration so far as we know to one important need of the profession. With the growth of large organizations of accountants, it has been necessary to establish a terminology to describe the various classes of employees in a way which will indicate something of the nature of their duty. We have had senior accountants, semi-senior accountants, junior accountants, managing accountants, and in-charge accountants, and the public is beginning to be a bit bewildered. The business man may be pardoned if he asks what is meant by an "in-charge" accountant, for example. Yet it is necessary that there should be some designation which will apply to the man who is sent out by a firm to take charge of an accounting engagement. He may be much more than a senior. What is he to be called? The term "in-charge" is at best a hyphenate, and its meaning may not be clear to the uninitiated. Many practitioners have given consideration to this question of terminology. So far the term "in-charge" seems to be the best that has been discovered and it is in general use in many offices. Here is a chance for some ingenious member of the profession to devote his summer leisure to the exploration of the field of philology and the capture of the perfect word descriptive of the accountant in charge.

Time Limit in Examinations

A correspondent in Texarkana, Texas, has written quite a long letter, commenting upon an editorial appearing in the June issue of this magazine under the title "An Instance of Misrepresentation." The burden of his criticism is the difficulty of examination—and this seems to apply to all examinations—and what he alleges to be the insufficient amount of time allowed for answering questions. He disclaims any wish to see the standards of examination lowered, but he points out many ways in which he believes improvement could be effected and the interests of candidates would be furthered. Some of these suggestions are immaterial, but on the one point of length of time allotted for each examination the correspondent is probably expressing the opinions of many who have undertaken to pass accounting examinations in all parts of the country. Consequently, it may be of curious significance to readers to learn the method adopted by the American Institute of Accountants in the preparation of questions and the safeguards which are set up to prevent anything like injustice or ambiguity. At several recent meetings of accountants officers of the Institute have explained in detail methods adopted by the board of examiners in preparing questions. The Institute's questions are used by the C. P. A. boards of thirty-four states and one territory, as well as by the Institute to test the qualifications of applicants for admission. This number of states, of course, constitutes the majority, and it is essentially important that in the setting and conduct of examinations there should be the closest possible approach to absolute fairness.

Preparing the Institute Examinations

The method adopted by the Institute's board of examiners as described by officers of the Institute may be summarized as follows: Several months before the date of examination the board of examiners communicates with officers of all state boards coöperating with the Institute, with all members of council of the Institute and with the members of the Institute committees, asking each one to submit for consideration of the board at least one question and its answer in practical accounting, theory of accounts and auditing. The Institute examiners themselves are expected to prepare questions for the consideration of the board. Out of the material thus accumulated, the board of examiners through a committee selects problems and questions for both sessions allowed for accounting and for the examination in auditing. The law questions are set by practising attorneys and reviewed by members of the Institute who are also members of the bar. After all these preliminary steps have been begun, the board of examiners calls in at least three men, members of the Institute, who are requested to answer the questions in the various subjects under actual examination conditions, and to keep a record of the time required for deliberate and comprehensive solution of each one. The results of this test are then compared, and if it be found that any one of the experimental examinees has required more than the time expected by the examiners, the questions are reduced in number or their difficulty modified so as to render it possible for each examinee to answer adequately in the time allowed.

Avoidance of Ambiguities

Furthermore, if it be found that there is a difference of opinion among the examinees as to the meaning of the language used or if it appears to either the committee of the board or the examinees that there is reasonable probability that the language will be misinterpreted, such amendments are made as will render the intention obvious. With the questions thus carefully tested and amended, the board proceeds to print and distribute the examination questions to the state boards coöperating. When applicants' papers are under consideration, the board gives credit for the intelligence displayed in answering, even if the answer may be absolutely wrong in detail. An applicant who shows a knowledge of the principles involved will not be penalized so heavily as would a candidate who by chance and without clear evidence of knowledge might have obtained something resembling the correct answer.

How the Grading Is Done

In grading the papers the Institute's examiners follow a definite system. One examiner is assigned to grading the answers to one problem or question submitted by all applicants throughout the country. By this means is brought about uniformity of judgment in regard to the qualifications of the applicants to answer each question. The results of examinations are compiled and the papers are then resubmitted to examiners for grading, and the matter is so arranged that each examiner will be called upon to grade the answers to questions other than those originally graded by him. The results are then compared, and where there is any material difference of opinion, the papers are carefully reviewed by other examiners and their decision is presented to the whole board. In the case of a few papers which are manifestly too far below the standard to be considered, the board does not give more than a cursory re-examination. The number of such papers, however, is usually quite small. By the methods which have been outlined in the foregoing paragraphs, the board of examiners believes that it has attained something resembling model procedure. No member of the board would probably venture to assert that the examinations are perfect. The perfect examination is, like human perfection, yet to be reached, but there should be no insuperable difficulty in the examinations prepared by the Institute to applicants who have had experience and have received sufficient preliminary education. There will always be a few men and women so seriously handicapped by extreme nervousness that they will not pass examinations. For such applicants the board of examiners may feel sympathy, but can find no relief. As has been said repeatedly in these editorial pages of THE JOURNAL, the world is still looking for a satisfactory substitute for examination as a test of ability.

A Collegiate Course in Accountancy

The development of accountancy education has been almost as remarkable as the development of public practice itself. In most of the great colleges and universities of the country in recent years departments have been established providing for instruction and education—and be it remembered the two things are not synonymous—in business and finance. In many cases, however, the amount of time devoted to the study of accountancy, pure and simple, has been regrettably small. Many excellent courses have been provided and it has been possible to obtain an immensely valuable knowledge of accountancy in most of the schools of commerce, but it is only recently that the hope of a course devoted exclusively to public accounting has been attained. The graduate school of business administration of Harvard university has now made arrangements for a half course or a full course in public-accounting practice and procedure. In the latest publication of the school the following description of the course is presented. This will be of interest to accountants and accounting instructors throughout the country, and it is hoped that in the near future many other colleges and universities will find it possible to follow the example of Harvard and establish courses leading directly to the professional practice of accountancy:

> "The purpose of the course is to study accepted practices and procedures with reference to the profession of public accountancy. During the first half-year the fundamentals of auditing are considered. The constructive audit will probably continue to be the most important work of the public accountant; in no field of accountancy is there a greater necessity for sound judgment, power of analysis, breadth of view, tact and resourcefulness than in auditing. Because of the comparative importance of the balance-sheet audit, the major portion of the first half-year is devoted to it; the detailed or cash audit is only briefly considered. Investigations for refinancing, for the determination of profits, and for other purposes have become of primary importance both to bankers and professional accountants, and are included in the year's work. Report writing and preparation of statements for the client are also studied. Other major activities of the professional accountant such as methods of devising and installing cost and financial accounting systems and budgetary control are next discussed. The internal organization of a public accounting firm, particularly with reference to the staff, the execution of work assigned, and the accounting methods, is briefly studied. Approximately a fourth of the year is given to closely supervised field work, whereby the student gains a first-hand knowledge of certain procedures of leading practitioners. Professional ethics is stressed throughout the course. Through the co-operation of prominent accounting firms, classroom discussion is based upon actual cases, presenting the most recent views of leaders in the profession."

Income-tax Department

EDITED BY STEPHEN G. RUSK

Twelve members of the board of tax appeals have been appointed by the president, five of whom were selected from the personnel of the bureau of internal revenue. Of the latter, two were members of the board of appeals and review. It is interesting to note that of the twelve members appointed, nine are lawyers, one is described as "executive officer of Kansas state farmers' union for many years; former newspaper man; and former member of faculty of Kansas university"; one an "accountant and authority on tax matters"; and one whose profession is not mentioned.

The revenue act empowers the president to appoint twenty-eight members, and it would seem to be in the interests of the long suffering taxpayer if a number of accountants of proved qualifications were made members of this important body. Congress in its wisdom deemed it meet that the salaries of members of this board should be limited to $7,500 per annum. In view of this limitation it is to be hoped that patriotic considerations will move a sufficient number of able men to undertake to render the invaluable services required of this board even if the financial emoluments are not alluring.

Mimeograph 3209 of recent issue amending article 836 of regulations 45 (1920 edition) and article 836 of regulations 62, gives detailed instructions as to retrospective appraisals for redetermining invested capital, March 1, 1913, value and fair cash value. The general lack of information that prevailed among taxpayers and their advisers in 1917 and 1918 was the cause of much, if not all, the defective tax returns turned in for those years. To one having the responsibility of protesting and appealing against the assessment of additional taxes for those years and reviewing them in the light of the present understanding of the provisions controlling the tax returns then made, it is amazing to contemplate the defects they contain. The errors made were detrimental to the interests of the taxpayer as frequently as they operated in his favor, and for reasons such as these, the information contained in this mimeograph becomes highly important even at this late date.

SUMMARY OF RECENT RULINGS

Proceeds of a life insurance policy do not constitute income and therefore are held not to be taxable under revenue act of 1918 (*U. S. v. Supplee Biddle Hardware Co.*)

Exchange of stock upon reorganization of a corporation held not to be a taxable transaction under the 1916 act (supreme court decision, *Weiss v. Stearn*)

Income of operating receivers of a corporation held to be subject to tax under provisions of revenue act of 1916.

Personal property tax assessed after death of decedent held not to be deductible for federal estate-tax purposes (*Hill, et al. v. Grissom*)

That income from California community property may be divided between husband and wife is being reconsidered by attorney general, his former opinion that it may be divided being withdrawn.

Time for filing fiscal-year returns of corporations, fiduciaries and partnerships has been extended to Sept. 15th (T. D. 3597), and time for filing capital-stock-tax returns is extended to September 30th. (Mim. 3206.)

March 1, 1913, value of property, though greater than cost, was used as basis of determining a loss upon the sale of the said property (*Vance v. McLaughlin*)

Taxpayer not allowed to enjoin another from delivering property to collector claiming under warrant of distraint (*Sramen v. Guaranty Trust Co. of N. Y.*)

Income of individuals acting as consultant of state or subdivision thereof, who are not regular employers, is subject to tax (*Metcalf et al. v. Mitchell*)

Students' Department

EDITED BY H. A. FINNEY

(Note.—The fact that these solutions appear in THE JOURNAL OF ACCOUNTANCY should not lead the reader to assume that they are the official solutions of the American Institute of Accountants. They merely represent the personal opinions of the editor of the *Students' Department.*)

AMERICAN INSTITUTE OF ACCOUNTANTS

EXAMINATION IN ACCOUNTING THEORY AND PRACTICE—PART II

MAY 16, 1924, 1 P. M. TO 6 P. M.

The candidate must answer all the following questions:

No. 1 (27 points):

Drafts of the profit-and-loss accounts and the balance-sheet of the Atlantic Trading Company, showing the results of operations for the year ended December 31, 1923, were prepared for submission to the directors in January, 1924.

Before they were approved, a report of an investigation of the accounts of the company for the years 1919, 1920 and 1921 was received from the internal-revenue department. This report reduced considerably the large amounts of depreciation written off various assets and made a claim for the difference as additional excess profits and income taxes.

The claim was subsequently paid, and the directors decided to have the accounts for the years 1922 and 1923 and the balance-sheets at the end of those years redrafted in order to bring them into agreement with the figures shown in the internal-revenue report.

The accounts on the books of the company appear as follows:

Property Accounts 1922	Valuation Jan. 1	Additions during year	Depreciation Dec. 31	Balance forward
Real estate.........	$200,503.79	$2,249.08*	$10,162.61	$192,590.26
Machinery and tools	2,206.95	1,799.01	1,918.07	2,087.89
Auto trucks........	21,521.06	31,000.48	12,360.08	40,161.46
Horse trucks........	132.50		132.50	
Horses.............	800.00	575.00	583.34	791.66
Harness............	245.70	61.05	221.75	85.00
Office furniture	1,774.42	2,909.86	1,610.59	3,073.69
	$227,184.42	$38,594.48	$26,988.94	$238,789.96
Property Accounts 1923				
Real estate.........	$192,590.26	$210.00*	$3,300.26	$189,500.00
Machinery and tools	2,087.89	1,235.38	1,755.73	1,567.54
Auto trucks........	40,161.46	8,782.41	17,134.84	31,809.03
Horse trucks........		112.58	66.92	45.66
Horses.............	791.66	700.00	741.67	749.99
Harness............	85.00	80.00	143.00	22.00
Office furniture	3,073.69	3,264.54	3,400.86	2,937.37
	$238,789.96	$14,384.91	$26,543.28	$226,631.59

* The additions to real estate in 1922 and 1923 apply to sheds.

The internal-revenue agents traced back the original costs of the assets and all additions. Against these total costs they created depreciation reserves at the rates shown below.

You are required to take their figures as at the date to which their examination was restricted (December 31, 1921) and to extend them further, on the same basis, to December 31, 1923. Then bring the amounts of total cost into the accounts of the company, create the necessary reserves for depreciation and state the adjustments required in the profit-and-loss accounts, surplus account and balance-sheets at December 31, 1922 and 1923, in order to show the effect of these changes.

The amounts of additions to the assets, stated in the books of the company for the years 1922 and 1923, are to be taken as correct.

Note that the item of real estate has been divided, by the internal-revenue agents, into three separate classes to show different rates of depreciation.

Summary of Report of Internal-Revenue Department Agents

	Total cost to Jan. 1, 1922	Depreciation reserve Jan. 1, 1922	Annual rate of depreciation allowed
Real estate (see below):			
Machinery and tools	$ 8,701.97	$ 4,306.77	20 %
Auto trucks	72,297.42	37,429.11	20 %
Horse trucks	1,691.63	680.39	$16\frac{2}{3}$%
Horses	5,788.17	2,873.07	20 %
Harness	1,444.59	1,116.92	$33\frac{1}{3}$%
Office furniture	5,576.92	1,311.03	10 %
Land } Real estate	164,364.60	(none)	(none)
Sheds } Real estate	9,581.14	1,578.11	10 %
Brick buildings } Real estate	39,596.93	2,143.88	2 %
		$51,439.28	
Depreciation reserve (not allocated to specific assets) for period prior to Jan. 1, 1919		12,718.36	
	$309,043.37	$64,157.64	

Solution:

The first step is to determine the adjusted values of the property, setting up the total costs in asset accounts and setting up the reserves against them. There does not seem to be any way of apportioning the unallocated reserve over the various classes of assets, as there is no information as to the dates of acquisition of the property.

ADJUSTMENT OF PROPERTY ACCOUNTS

As of January 1, 1922

		Corrected valuations		
	Valuation per books	Total cost	Depreciation reserve	Net value
Real estate...........	$200,503.79			
Land............		$164,364.60		$164,364.60
Sheds............		9,581.14	$1,578.11	8,003.03
Brick buildings....		39,596.93	2,143.88	37,453.05
Machinery and tools...	2,206.95	8,701.97	4,306.77	4,395.20
Auto trucks..........	21,521.06	72,297.42	37,429.11	34,868.31
Horse trucks..........	132.50	1,691.63	680.39	1,011.24
Horses...............	800.00	5,788.17	2,873.07	2,915.10
Harness..............	245.70	1,444.59	1,116.92	327.67
Office furniture........	1,774.42	5,576.92	1,311.03	4,265.89
Depreciation reserve (not allocated to specific assets) for period prior to January 1, 1919..............			12,718.36	12,718.36*
Total........	$227,184.42	$309,043.37	$64,157.64	$244,885.73
Adjustments as of January 1, 1922:				
Property account before adjustment		227,184.42		
Debit to property account........		$81,858.95		
Reserves for depreciation — before adjustment.....				
Credits to reserves			$64,157.64	
Net value of property before adjustment.......				227,184.42
Credit to surplus..				$17,701.31

The problem indicates that the property accounts have already been adjusted as of January 1, 1922, and that adjustments have also been made in regard to the taxes, as the problem states that the taxes were paid. In computing the depreciation for 1922 and 1923 on the adjusted basis, it is necessary to take precautions against over-depreciating any asset. By reference to the following schedule, it will be noted that depreciation of only $327.67 was provided on the harness acquired prior to January 1, 1922. Depreciation at the rate of 33⅓% would have amounted to $481.53, which would have over-depreciated the property.

* Deduction.

ADJUSTMENT OF PROPERTY AND OTHER ACCOUNTS
As of December 31, 1922

	(1) Depreciation rate	(2) Total cost to Jan. 1, 1922	(3) Depreciation thereon for 1922	(4) Depreciation prior to 1922	(5) Total reserve against assets acquired prior to 1922
Real estate:					
Land		$164,364.60			
Sheds	10%	9,581.14	$958.11	$1,578.11	$2,536.22
Brick buildings	2	39,596.93	791.94	2,143.88	2,935.82
Machinery and tools	20	8,701.97	1,740.39	4,306.77	6,047.16
Auto trucks	20	72,297.42	14,459.48	37,429.11	51,888.59
Horse trucks	16⅔	1,691.63	281.94	680.39	962.33
Horses	20	5,788.17	1,157.63	2,873.07	4,030.70
Harness	33⅓	1,444.59	327.67	1,116.92	1,444.59
Office furniture	10	5,576.92	557.69	1,311.03	1,868.72
Unallocated reserve				12,718.36	12,718.36
		$309,043.37	$20,274.85	$64,157.64	$84,432.49

	(6) Cost of property acquired during 1922	(7) Depreciation one half year	(8) Total property (2+6)	(9) Total reserve (5+7)
Real estate:				
Land			$164,364.60	
Sheds	$2,249.08	$112.45	11,830.22	$2,648.67
Brick buildings			39,596.93	2,935.82
Machinery and tools	1,799.01	179.90	10,500.98	6,227.06
Auto trucks	31,000.48	3,100.05	103,297.90	54,988.64
Horse trucks			1,691.63	962.33
Horses	575.00	57.50	6,363.17	4,088.20
Harness	61.05	10.18	1,505.64	1,454.77
Office furniture	2,909.86	145.49	8,486.78	2,014.21
Unallocated reserve				12,718.36
	$38,594.48	$3,605.57	$347,637.85	$88,038.06

Property account:		
Total cost (per column 8)		$347,637.85
Property account per books (as stated in problem)		238,789.96
Addition to property account		$108,847.89
Consisting of:		
Correction as of January 1, 1922	$81,858.95	
Depreciation written off in 1922	26,988.94	
Total	$108,847.89	
Reserves for depreciation—total credit (column 9)		$88,038.06

Consisting of:		
Reserve as of January 1, 1922		$64,157.64
Depreciation for 1922:		
On assets acquired prior to 1922	$20,274.85	
On assets acquired during 1922	3,605.57	23,880.42
Total		$88,038.06
Decrease of depreciation and increase of profits of 1922:		
Depreciation provided per books		$26,988.94
Adjusted amount provided		23,880.42
Decrease in depreciation and increase in profits		$3,108.52
Additional federal taxes:		
12½% of additional profits of $3,108.52		$388.57
Surplus:		
Addition to property	$108,847.89	
Less addition to reserve	88,038.06	
		$20,809.83
Less additional taxes		388.57
Net addition to surplus		$20,421.26

Summary of additions to balance-sheet items
As of December 31, 1922

Property account	$108,847.89	Reserves for depreciation	$88,038.06
		Additional tax liability	388.57
		Surplus	20,421.26
	$108,847.89		$108,847.89

The following tabulation continues the computations and shows the values at the end of 1923, after adjustments:

Adjustment of Property and Other Accounts

As of December 31, 1923

	(1) Depreciation rates	(2) Total cost to January 1, 1922	(3) Reserve to Dec. 31, 1922	(4) Depreciation thereon for 1923
Real estate:				
Land		$164,364.60		
Sheds	10%	9,581.14	$2,536.22	$958.11
Brick buildings	2	39,596.93	2,935.82	791.94
Machinery and tools	20	8,701.97	6,047.16	1,740.39
Auto trucks	20	72,297.42	51,888.59	14,459.48
Horse trucks	16⅔	1,691.63	962.33	281.94
Horses	20	5,788.17	4,030.70	1,157.63
Harness	33⅓	1,444.59	1,444.59	
Office furniture	10	5,576.92	1,868.72	557.69
Unallocated reserve			12,718.36	
		$309,043.37	$84,432.49	$19,947.18

	(5) Total reserve thereon (3+4)	(6) Additions 1922	(7) Depreciation thereon for 1922	(8) Depreciation thereon for 1923
Real estate:				
Land				
Sheds	$3,494.33	$2,249.08	$112.45	$224.91
Brick buildings	3,727.76			
Machinery and tools	7,787.55	1,799.01	179.90	359.80
Auto trucks	66,348.07	31,000.48	3,100.05	6,200.10
Horse trucks	1,244.27			
Horses	5,188.33	575.00	57.50	115.00
Harness	1,444.59	61.05	10.18	20.35
Office furniture	2,426.41	2,909.86	145.49	290.99
Unallocated reserve	12,718.36			
	$104,379.67	$38,594.48	$3,605.57	$7,211.15

	(9) Additions 1923	(10) Depreciation thereon for 1923	(11) Total property (2+6+9)	(12) Total reserve (5+7+8+10)
Real estate:				
Land			$164,364.60	
Sheds	$210.00	$10.50	12,040.22	$3,842.19
Brick buildings			39,596.93	3,727.76
Machinery and tools	1,235.38	123.54	11,736.36	8,450.79
Auto trucks	8,782.41	878.24	112,080.31	76,526.46
Horse trucks	112.58	9.38	1,804.21	1,253.65
Horses	700.00	70.00	7,063.17	5,430.83
Harness	80.00	13.33	1,585.64	1,488.45
Office furniture	3,264.54	163.23	11,751.32	3,026.12
Unallocated reserve				12,718.36
	$14,384.91	$1,268.22	$362,022.76	$116,464.61

Property account:		
Total cost (per column 11)		$362,022.76
Property account per books (per problem)		226,631.59
Addition to property account		$135,391.17
Consisting of:		
Correction as of December 31, 1922	$108,847.89	
Depreciation written off in 1923	26,543.28	
Total	$135,391.17	
Reserves for depreciation—Total (per column 12)		$116,464.61
Consisting of:		
Reserves as of December 31, 1922		$88,038.06
Depreciation for 1923:		
On assets acquired prior to January 1, 1922	$19,947.18	
On assets acquired during 1922	7,211.15	
On assets acquired during 1923	1,268.22	28,426.55
Total		$116,464.61

Increase of depreciation and decrease of profits for 1923:	
Adjusted depreciation	$28,426.55
Depreciation per books	26,543.28
Decrease in depreciation and increase in profits	$1,883.27
Reduction of taxes—12½% of $1,883.27	$235.41
Surplus:	
Addition as of December 31, 1922	$20,421.26
Addition on account of decrease in taxes—1923	235.41
Total	$20,656.67
Less additional depreciation—1923	1,883.27
Net increase in surplus as of December 31, 1923	$18,773.40

Summary of additions to balance-sheet items

As of December 31, 1923

Property	$135,391.17	Reserves for depreciation	$116,464.61
Claim for overpayment of 1923 federal taxes	235.41	Additional tax liability —1922	388.57
		Surplus	18,773.40
	$135,626.58		$135,626.58

No. 2 (10 points):

A certain manufacturing concern makes tools and other equipment for use in its own plant and charges them to the capital asset accounts at the market value (which is in excess of cost) and credits the difference between the market and the cost value to profit-and-loss for the period in which the tools and other equipment are manufactured.

In the examination of the customers' accounts of this concern, you find certain credit balances aggregating $13,011.31 arising out of allowances for returned goods, defective goods, etc. It has been the practice of the company to deduct items of this nature from amounts due from customers and to state the net difference in the balance-sheet as "uncollected customers' accounts."

What is your criticism of these methods?

Solution:

The practice of charging the property accounts with the market value of tools and other equipment manufactured, such market value being in excess of cost, and crediting the excess over cost to profit-and-loss for the period, is subject to two criticisms. In the first place, it results in carrying fixed assets in the accounts at a value greater than cost, which is incorrect in itself and results in the further error of making the depreciation charges of subsequent periods too heavy. In the second place, it results in taking up a profit which has not been realized. Profits are made by sales, and not by manufacturing fixed assets for use in further production. The manufacture of the tools and equipment has evidently resulted in a saving, but savings should not be recorded as profits. Since credit balances in accounts receivable are liabilities, they should be set out on the liability side of the balance-sheet, and the debit side should show accounts receivable at the total of the debit balances in the subsidiary ledger.

No. 3 (23 points):

The following is a summary of the cash receipts and disbursements of the trustees of the late R. A. Armstrong and a distribution of the estate.

Under the terms of his will, Mr. Armstrong left all his estate in trust for his two children with the exception of his life insurance of $500,000 and his home, valued at $100,000, which he bequeathed to his widow, an annuity to his sister and sundry legacies. The income from the estate he instructed the trustees to pay to his widow during her life.

Receipts:

Cash and bank balances at date of death	$50,000
Life insurance	500,000
Income from bond interest	5,000
Income from dividends on stock	10,000
Income from dry-goods business, net	500,000
Sundry debtors at date of death	15,000
Proceeds of sale of dry-goods business, including new buildings and equipment	5,500,000
Securities sold, stocks and shares	1,000,000
Securities sold, bonds and debentures	500,000
	$8,080,000

Disbursements:

Sundry creditors at date of death	$5,000
Inheritance tax	800,000
Sundry legacies paid in full	300,000
Mrs. Armstrong, net income	300,000
Advances to heirs ($100,000 each)	200,000
Legal expenses	400,000
Funeral expenses	15,000
Cost of constructing extension, dry-goods store	700,000
Cost of annuity for Miss Armstrong, deceased's sister	500,000
	$3,220,000

Balance, being net amount of estate to be divided equally between the two children	$4,860,000

From the figures and information given above, you are asked to prepare correct capital and revenue accounts and state the balance due to the widow and each of the children. (Consider that the widow should receive all the income collected.)

Solution:

In order to maintain a proper distinction between principal and income, the cash account should have been provided with classification columns as follows:

Cash receipts	Principal	Income	Total
Cash and bank balances at time of death	$50,000		$50,000
Life insurance	500,000		500,000
Income from bond interest		$5,000	5,000
Income from dividends on stock		10,000	10,000
Income from dry-goods business—net		500,000	500,000
Sundry debtors at date of death	15,000		15,000
Proceeds of sale of dry-goods business	5,500,000		5,500,000
Securities sold, stocks and shares	1,000,000		1,000,000
Securities sold, bonds and debentures	500,000		500,000
	$7,565,000	$515,000	$8,080,000

Cash disbursements			
Sundry creditors at date of death	$ 5,000		$ 5,000
Inheritance tax	800,000		800,000
Sundry legacies	300,000		300,000
Mrs. Armstrong—net income		$300,000	300,000
Advances to heirs	200,000		200,000
Legal expenses	400,000		400,000
Funeral expenses	15,000		15,000
Cost of extension, dry-goods store	700,000		700,000
Cost of annuity for Miss Armstrong	500,000		500,000
Balance	4,645,000	215,000	4,860,000
	$7,565,000	$515,000	$8,080,000

The problem specifically states that the bond interest and the dividends were income. It is unusual to find an estate with no interest accrued at the date of death, and with no dividends declared at that time. In classifying the income from the dry-goods business as "income" it is necessary to assume that the wording of the problem is final and that the books were closed at date of death. There is no basis for dividing the legal expenses between principal and income, as there is no information as to the amount incurred in preserving and realizing the estate and the amount incurred in collection of income. There is no evidence to indicate that the trustees had any right to make advances to the heirs.

It may be impossible to prepare an absolutely correct capital account from the information given. The estate, or capital, account should be credited with the inventoried value of the property at the time of death; subsequent gains and losses on realization should be credited and charged to the account. But this information is not given. The income account would be credited with the items in the income column of the cash receipts record, and charged with the items in the income column of the cash disbursements record. The table, as prepared, shows that Mrs. Armstrong has not received the net income but is entitled to an additional payment of $215,000.

No. 4 (23 points):

You are instructed to investigate the financial condition of a concern by a client who is a large creditor. He informs you that the company about to be investigated has been falling behind in payments and believes that this is caused by a too extensive application of funds, or use of working capital, for the construction of new plants, etc. He furnishes you with a statement supplied by an officer of the company as at the beginning of the year, on the basis of which credit was granted, and requests that you make a report on the financial standing of the concern at the end of the year and on the situation in general.

You find that the company has no general ledger, but that a cashbook, sales book, voucher register and accounts-receivable ledger are kept. You list the assets and liabilities, with the exception of the plant (of the cost of which there is no record in evidence), and obtain the following result of conditions as at the end of the year:

Cash	$ 5,000	Bank loans	$ 14,000
Accounts receivable	24,000	Notes payable	20,000
Inventories	18,000	Vouchers payable	75,000
Sundry assets	4,000	Mortgages payable	10,000
Total assets, excepting plant	$51,000	Total liabilities, excepting capital	$119,000

The balance-sheet, presented by the officer representing the company, at the beginning of the year was as follows:

Cash	$ 40,000	Bank loans	$ 10,000
Accounts receivable	38,000	Notes payable	15,000
Inventories	20,000	Vouchers payable	60,000
Sundry assets	4,000	Mortgages payable	10,000
Plant	250,000	Capital stock	50,000
		Surplus	207,000
	$352,000		$352,000

An analysis of the books of original entry for the year furnished the following summarized results:

Cashbook receipts:		
Cash	$852,500	
Discount	7,500	
To accounts receivable		$850,000
Bank loans		10,000
Cashbook disbursements:		
Vouchers payable	838,500	
Bank loans payable	16,000	
To cash		854,000
Discount		500
Sales book:		
Accounts receivable	852,000	
To sales		852,000
Voucher register:		
New construction	25,000	
Operating expenses	798,000	
To vouchers payable		823,000

From trustworthy information, it was gathered that the inventories had decreased $5,000 during the year.

Having completed your investigation and reached conclusions for the purpose intended, what will be the report to your client?

Solution.

The report might begin with a comparative statement of assets and liabilities, showing the condition at the beginning and at the end of the year. The statement as of the beginning of the year would show the figures submitted by the officer of the company, with a comment as to the source of the information. In the following statement the plant value as of the beginning of the year has been added to the expenditures for plant made during the year, but the report should contain a qualification disclaiming responsibility for the $250,000 value.

NAME OF COMPANY

Comparative Balance-Sheet—Dates

Assets	End	Beginning	Increase Decrease*
Cash	$ 5,000	$ 40,000	$35,000*
Accounts receivable	24,000	38,000	14,000*
Inventories	18,000	20,000	2,000*
Sundry assets	4,000	4,000	
Plant:			
Value at beginning of year	250,000	250,000	
Additions during year	25,000		25,000
	$326,000	$352,000	$26,000*

Liabilities			
Bank loans	$14,000	$10,000	$4,000
Notes payable	20,000	15,000	5,000
Vouchers payable	75,000	60,000	15,000
Mortgages payable	10,000	10,000	
Capital stock (presumably no change)	50,000	50,000	
Surplus	157,000	207,000	50,000*
	$326,000	$352,000	$26,000*

The summary of the entries for the year indicates that the assets and liabilities shown in the statement furnished by the officer of the company as of the beginning of the year were misstated, because the changes in assets and liabilities shown in the increase-decrease column of the foregoing comparative statement do not agree with the changes shown by the books of original entry, as summarized below:

Cash:		
Disbursements		$854,000
Receipts		852,500
Net decrease		$1,500
Accounts receivable:		
Charges for sales		$852,000
Credits:		
Cash	$842,500	
Discount	7,500	850,000
Net increase		$2,000
Bank loans:		
Cash paid during the year		$16,000
Cash received during the year		10,000
Net decrease		$6,000
Vouchers payable:		
Charges during the year:		
Cash	$838,000	
Discount	500	$838,500
Credits during the year:		
New construction	25,000	
Operating expenses	798,000	823,000
Net decrease		$15,500

Assuming that the balance-sheet at the end of the year and the entries during the year have been verified by audit, the balance-sheet at the beginning of the year can be built up by applying to the closing balance-sheet the increases and decreases shown by the books of original entry. The following statement shows the balance-sheet submitted by the officer and the balance-sheet built up by the method suggested. There is no indicated change in the notes payable. The inventory has decreased $5,000.

NAME OF COMPANY

Comparative Balance-Sheet

Assets	End	Increase Decrease*	*Beginning* Adjusted	Per officer
Cash	$5,000	$1,500*	$6,500	$40,000
Accounts receivable	24,000	2,000	22,000	38,000
Inventories	18,000	5,000*	23,000	20,000
Sundry assets	4,000		4,000	4,000
Plant (assuming accuracy of $250,000)	275,000	25,000	250,000	250,000
	$326,000	$20,500	$305,500	$352,000
Liabilities				
Bank loans	$14,000	$6,000*	$20,000	$10,000
Notes payable	20,000		20,000	15,000
Vouchers payable	75,000	15,500*	90,500	60,000
Mortgages payable	10,000		10,000	10,000
Capital stock	50,000		50,000	50,000
Surplus	157,000	42,000	115,000	207,000
	$326,000	$20,500	$305,500	$352,000

The increase in surplus during the year, in the amount of $42,000, is supported and accounted for by the following statement:

Name of company

Profit and loss account

For the year ended ——

Inventory at beginning	$23,000	Sales	$852,000
Operating expenses	798,000	Discounts taken	500
Discounts allowed	7,500	Inventory at end	18,000
Profit	42,000		
	$870,500		$870,500

The reasons for the company's inability to meet its payments may be further explained by the following statement:

Name of company

Statement of application of funds

For the year ended ——

Funds provided:		
By profits		$42,000.00
By net decrease in current assets:		
Decrease in cash	$1,500.00	
Decrease in inventories	5,000.00	
Total	$6,500.00	
Increase in accounts receivable	2,000.00	
		4,500.00
		$46,500.00

Funds applied:

Additions to plant		$25,000.00
Decreases in current liabilities:		
Bank loans	$6,000.00	
Vouchers payable	15,500.00	
		21,500.00
		$46,500.00

No. 5 (17 points):

The following propositions are presented:

1. Depreciation of physical property is continuous and unavoidable.
2. Interest on invested capital is an element of cost.
3. Cash is a current asset.
4. True value of inventories is cost or market, whichever is lower.
5. True value of fixed assets on the books of a going concern is replacement value.
6. Interest paid previous to operation of a new plant is part of cost of plant.
7. Dividends on stocks accrue day by day.
8. Inter-company profits belonging to minority stockholders have no place in a consolidated balance-sheet.

Without copying or discussing the foregoing propositions at any length, indicate to which of the categories following they belong:

A. Statements of incontrovertible fact, or
B. Statements which are not strictly true.
C. Statements of accepted accounting principle or procedure which are correct, or
D. Statements of accepted accounting principle or procedure which are incorrect, or
E. Controversial statements of accounting principle or procedure for which reputable authority may be found on both sides.

Solution:

(1) Statement of incontrovertible fact.

(2) Controversial statement.

(3) Statement of incontrovertible fact so far as unrestricted cash is concerned. Cash in sinking fund is not current.

(4) Until recently this statement would have been considered an expression of accepted accounting principle which was regarded as correct. Other propositions have been submitted by competent authorities recently which perhaps put the statement in the controversial class.

(5) This is a statement which is not strictly true. Replacement value is perhaps not true value, but most accountants recognize the propriety of reflecting replacement value in the accounts if proper treatment is given to the unrealized profit resulting from revaluing the property.

(6) This statement is not strictly true. The interest is not in reality a part of the cost, but the capitalization of the interest is permitted because of the fact that before a new plant is put into operation it produces no profits against which the interest can be charged.

(7) This statement is not legally true. Dividends do not accrue. But since the so-called accrual of dividends is taken into account in the purchase and sale of stock it can scarcely be denied that the passing of time tends to add a value to the stock. Perhaps the best statement is: It is unfortunate that there is no other word which expresses the real meaning which "accrual" is called upon to express.

(8) This is a controversial question. Some accountants believe that the entire inter-company profit should be eliminated; others believe that only the holding company's proportion should be eliminated.

Reserves for Contingencies

Editor, Students' Department:

Sir: On the books of a partnership there appears at the end of three years the following account: "Reserve for possible losses of perishable merchandise, $4,500." The partnership was formed by A, B and C, who share profits and losses equally.

The partnership agreement states that goodwill shall be considered as an amount equal to the net earnings for the last two years. At the end of the third year A desires to retire from the partnership. The reserve was created out of the profits of the two previous years, and at the time of A's retirement it is apparent that the reserve has not been needed as no losses of merchandise have occurred. Is the retiring partner entitled to a share of the reserve?

S. D. G.

Rio Piedras, Porto Rico.

The retiring partner is entitled to share in the reserve. It is not proper to deduct from the profits of the three years during which he was a partner a provision for a loss which has not occurred during the period of his membership in the firm. If any merchandise on hand at the time of his retirement is in bad condition, the loss should be charged against the reserve. The question seems to mean that the merchandise is in good condition.

A will share in the reserve in two ways. In the first place, since profits and losses are shared equally, he will be entitled to a credit of one-third of the amount of the reserve as his share of the profits which have been set aside in a contingent reserve which proved to be unnecessary. In the second place, the reserve will have to be added back to the profits of the past two years to determine the total profits on which the good-will is based. This will result in an increase of $4,500 in the good-will and, as good-will is divisible in the profit and loss ratio, A will be entitled to one-third of the good-will.

Thus A will receive an additional credit of $1,500 as his share of the profits set aside in the reserve and an additional $1,500 as his share of the increase in the good-will.

Consignments and Bonus

Editor, Students' Department:

Sir: An employee is entitled to a commission or bonus of two and one-half per cent of the annual net profits. He leaves the firm on April 1, 1924. The profit for 1923 was say $20,000. Goods shipped during 1923 on consignment and billed at regular prices, to be accounted and paid for when sold, amounted to say $15,000. These goods were taken into the inventory at December 31, 1923, at cost.

Is the employee entitled to two and one-half per cent on the earnings from consignments shipped during 1923 and collected up to April 1, 1924?

Very truly yours,

F. C. A.

New York.

In answering this question it must first be known whether the employee is to be allowed a commission on the profits earned between December 31, 1923 and April 1, 1924. If he is to be allowed such a commission, it would seem that he should be allowed the two and one-half per cent on the profits earned on consignments closed during the three months.

But if he is not to receive any bonus on the 1924 profits, it seems equally clear that he is not entitled to any bonus on consignments shipped during 1923 but not sold by consignees until 1924. The principle is well established that profits are earned by sales and no profit is made by merely shipping goods on consignment. Therefore, the shipments which took place in 1923 produced no profit during that year unless they were closed during the year; the profits on consignments closed during 1924 belong to 1924.

On the other hand the employee would have the right to demand that all expenses in connection with these consignments be deferred until 1924, as it is not proper for him to suffer by the incurring of expenses if he is not allowed to benefit by profits. It may also be possible that the employee is entitled to some special consideration because of the fact that he devoted time and labor to inducing consignees to take the goods.

Partnership Adjustment

Editor, Students' Department:

SIR: Through the columns of THE JOURNAL OF ACCOUNTANCY, kindly give me your opinion of the solutions of the following problems, and if both are incorrect, will you please give me the proper one?

"A and B are partners sharing profits in accordance with their original investments. A invested $5,000 and B $3,000, making the capital of the firm $8,000. They sell a one-third interest in the business to C for $8,000. How shall A and B divide the $8,000 received from C so that each may retain a one-third interest in the business without increasing or decreasing the original capital of the firm?"

Solution No. 1:

A owns 5/8 or 15/24 of the business.
B owns 3/8 or 9/24 of the business.
A retains 1/3 or 8/24 of the business, therefore A contributes to C's share with 7/24 (15/24 less 8/24).
B retains 1/3 or 8/24 of the business, therefore B contributes to C's share with 1/24 (9/24 less 8/24).
Now if C pays $8,000 for 8/24 of the business, he pays $1,000 for 1/24.

If A contributes 7/24 he will receive	$7,000
If B contributes 1/24 he will receive	1,000
Total	$8,000

Solution No. 2.

	A	*B*	*C*	*Total*
Original capital	$5,000.00	$3,000.00		$8,000.00
A's contribution to C's share: 5/8 of 1/3, or 5/24 of $8,000	1,666.67		$1,666.67	
B's contribution to C's share: 3/8 of 1/3, or 3/24 of $8,000		1,000.00	1,000.00	
Capitals after contributions	$3,333.33	$2,000.00	$3,666.57	$8,000.00
A's contribution to equalize B's capital	666.66	666.66		
New capitals	$2,666.67	$2,666.66	$2,666.67	$8,000.00

A's share in the $8,000 contributed by C is:

5/8 of $8,000, or	$5,000.00
Capital contributed to B	666.66
Total amount to be received in cash	$5,666.66

B's share in the $8,000 contributed by C is:	
3/8 of $8,000, or	$3,000.00
Capital repaid to A	666.66
Total amount to be received in cash	$2,333.34

Thanking you in advance for your courtesy, I remain,

Yours very truly,
S. G. RAMIREZ.

San Juan, Porto Rico.

The price received from C should be divided into two parts: first, the compensation for the interests transferred, and secondly, the profit. The first portion should be divided on the basis of the interests transferred and the second portion should be divided in the profit and loss ratio. The profit and loss ratio governs the division of the profit on a sale of an interest, because the partners are taking an immediate profit instead of waiting to take it from operations. In other words, they are allowing a third partner a share in the profits. This will decrease the profits to be shared in the future by the original partners. Therefore the profit on the sale should be divided in the ratio which would have governed the division of the profits parted with.

The first solution is therefore wrong because it divided the entire price on the basis of the interests transferred. The second solution is correct, but it is not tabulated in what appears to be a clear manner. The following statement of facts is suggested:

STATEMENT OF DIVISION BETWEEN A AND B OF CASH RECEIVED FROM C

		A	*B*	*Total*
Original capitals		$5,000.00	$3,000.00	$8,000.00
Less capitals retained—1/3 of $8,000.00		2,666.67	2,666.67	5,333.34
Cash to be received for capital interests transferred		$2,333.33	$333.33	$2,666.66
Cash to be received for profit on transfer:				
Total amount received	$8,000.00			
Total capital transferred	2,666.66			
Profit	5,333.34			
Divided in the profit and loss ratio:				
A—5/8 of $5,333.34		3,333.34		
B—3/8 of 5,333.34			2,000.00	
Total				5,333.34
Total cash to be received		$6,666.67	$2,333.33	$8,000.00

Book Reviews

AUDITING AND ACCOUNTING HANDBOOK, by FREDERIC W. KILDUFF, *McGraw-Hill Book Company, Inc.*, New York. 813 pp.

The purpose of the *Auditing and Accounting Handbook*, as stated by the author in his preface, is to address to those engaged in the practice of auditing and accounting a handbook in which are to be found "important and reliable tables, classifications, schedules, digests, formulas, and other valuable information applicable to auditing and accounting, which those so engaged may use as a convenient means for simplifying and solving their problems." In short, it is intended to be a book of reference, not a text-book. It is assumed that the user already knows *how*. Training and experience may give one full knowledge how to make an audit, but only carefully prepared programmes and schedules will guard against oversights due to brain-fag in a long audit. The longer our experience, the more we are apt to depend upon it and omit this safeguard, particularly in a busy season. In the first two sections of this handbook Mr. Kilduff offers complete auditing programmes and schedules with full notations of all the essential facts to be ascertained. At the close of an engagement a rapid check of these sections should satisfy one that he has not overlooked anything. Section 3 contains an outline of the procedure for making a plant survey. This is a class of work not often encountered, but at least a perusal of this section might prevent a novice from attempting a job beyond his powers. Sections 4 and 5 deal with the inventory and property classifications and records. Besides the instructions as to the steps to be taken, these sections contain voluminous lists of the articles and units usually to be found, the property lists including also rates of depreciation. Other sections, 6 to 9, cover depreciation methods, financial statements and forms, accounts and accounting forms, and mathematics, the last containing many time-saving formulas. In section 10, covering over 300 pages, will be found an amazing amount of information and tables of all kinds sure to be useful to the accountant at some time or other. The final section, 11, on federal taxes, might well have been omitted, considering the complexities and continual changing of the income tax laws. A good index closes the book. Binding, paper and print are all that can be asked in a book that must stand long usage.

W. H. LAWTON.

DEPRECIATION PRINCIPLES AND PRACTICE, by E. A. SALIERS. *The Ronald Press Company*, New York. 590 pp.

Depreciation Principles and Practice is a revision and expansion of the author's earlier work, *Principles of Depreciation*. The more significant additions relate to the treatment of depreciation in the federal income-tax regulations and by the courts in valuation proceedings; however, nearly every topic treated in the smaller book has been amplified in this volume. Furthermore, five appendices of considerable proportions have been added to the new publication. The present volume, which is divided into four general sections, is, in the reviewer's opinion, much better organized than was the earlier treatise. The general divisions of the present volume are: general principles, depreciation and the income tax, depreciation and public-utility valuation and appendix. Appendices A, B and C relate respectively to depreciation of oil and gas equipment, depreciation and I. C. C. railroad valuation, and mine valuation (this latter being extracts from a letter received from the deputy commissioner of internal revenue). Appendix D is a copy of bulletin "F" *Depreciation and Obsolescence*, issued by the bureau of internal revenue, August 31, 1920. Appendix E, consisting of 78 pages, is given to the depreciation rates of specific assets; while not comparable to the depreciation materials contained in the *Accountants' Index*, it will be found of practical assistance to anyone needing such information.

The book, particularly that section of it dealing with public utility valuation, contains materials available only as a result of careful and continuous research. The section on the income tax also shows genuine familiarity with the law and regulations. So many controversial points exist regarding depreciation that it can scarecely be expected that readers will agree on many points with the author; on the whole, however, the book is thought-provoking and well worth a place on the accountant's bookshelf.

J. HUGH JACKSON.

COST ACCOUNTS, by GEORGE HILLIS NEWLOVE, *White Press, Inc.*, Washington, D. C. 183 pp.

"Control Accounts for Cost Records" would better describe this book, placing it in its proper field, that of general accounting, and fitting as well into the author's purpose of introducing the student to the subject of cost accounting. It is merely a text book and rather narrow in its application. Notwithstanding that in the preface it purports to specialize on the "how" of cost accounting, it does not go beyond the confines of the general ledger. It is a book for the student only and needs to be supplemented by instruction from an experienced teacher.

GEORGE REA.

ACCOUNTING PROBLEMS; ADVANCED, by CHARLES F. RITTENHOUSE and ATLEE L. PERCY. *McGraw-Hill Book Co., Inc.* 398 pp.

The authors of this book presumably do not intend that it shall be used as a text, because the discussion of principles and of methods of procedure is meager. The intention is rather to provide a laboratory manual containing carefully selected supplementary exercises to be used with a text or by an instructor who uses the lecture method instead of the text method. There are some two hundred problems and eighty questions, dealing with consolidations, receiverships, estates, railways, public utilities, municipalities, banks, colleges and similar institutions, costs, actuarial science, foreign exchange, partnerships, income taxes and other miscellaneous subjects. Some of the problems have been constructed by the authors for pedagogical reasons to cover points not brought out in problems set in the American Institute and in the state C. P. A. examinations, but most of the problems have been selected from these sources. There is no indication as to whether solutions are available for the use of classes or of men preparing by private study for the examinations.

H. A. Finney.

Current Literature

Compiled in the Library of the American Institute of Accountants

[Photostatic reproductions (white printing on a black background) of most of the articles listed in THE JOURNAL OF ACCOUNTANCY or *Accountants' Index* may be obtained from the library of the American Institute of Accountants, 135 Cedar Street, New York, at a rate of 25 cents a page (8½ in. x 11 in.), at 35 cents a page (11½ in. x 14 in.) plus postage. Members and Associates of the American Institute of Accountants are entitled to a discount of 20 per cent. Indentify the article by author, title, name of periodical in which it appeared, date of publication and paging. Payment must accompany all orders.]

ACCOUNTANCY

Sells, Elijah Watt. *Natural Business Year and Thirteen Other Themes.* Chicago, A. W. Shaw Company, 1924. 276 p.

Contents: Natural Business Year for Inventories and Fiscal Closings; You Can't Judge Your Business by the Past Three Years; Certified Public Accountancy as a Profession; Accounting Profession: Its Demands and Its Future; Cost Accounting; Accountant of 1917; What Shall Be Done to Put Education for Accountancy on a Professional Basis?; Inaugural Address; Publicity of Financial Affairs of Corporations; Corporate Management Compared with Government Control; Why Not Lessen the Evils of Present Taxation; Plan for International Peace; Proposed Plan for Handling Interline Freight Claims.

Law

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