

2-1922

Book Reviews

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Recommended Citation

Lawton, W. H. (1922) "Book Reviews," *Journal of Accountancy*. Vol. 33: Iss. 2, Article 8.

Available at: <https://egrove.olemiss.edu/jofa/vol33/iss2/8>

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Book Reviews

AUDITING THEORY AND PRACTICE, vol. I, General Principles, by ROBERT H. MONTGOMERY. *The Ronald Press Co.*, New York. 730 pp. Cloth.

The increasing importance and complexities of scientific auditing are well indicated by the growth of Montgomery's *Auditing*, now in its third edition. The second edition of 1916 contained 900 pages, including 150 devoted to the income tax. The first volume of this, the third edition, has 730 pages devoted entirely to general principles of auditing, and it is to be followed by a second volume which will deal with special procedures applicable to various classes of business. And yet there are some who maintain that accountancy has made little progress in the last twenty years!

If there is any point in general auditing principles not covered in this edition we have failed to discover it. True, we were a little disappointed to find no definite advice as to an auditor's duty to disclose to his client A information of value which he has incidentally obtained from client B. The advice given on page 568 (which has a slightly ironical sound) may be good, but we can hardly imagine an auditor telling a client in advance that any evidence of "graft" in his books will be reported to the injured party, if the latter happens to be a client also! But that is not exactly the point we raise, which is: Is it ethical for an auditor to use such information if it is likely to injure a former client, or, vice versa, to suppress it if it is likely to work to the detriment of his present client?

With the abnormal conditions of 1918 to 1921 in mind every purchaser of the present edition will probably turn, as the reviewer did, to the chapters on inventories. We have all had to do more or less violence to our professional consciences and we look for approval or condemnation to the author. When we find he is just as human as the rest of us, we are sadly torn between relief and dismay—relief, that our own straying from the path of strict rectitude may be considered "good accounting practice"—dismay, to find our faith in the inflexible standard of "cost or market" shaken to its foundations! We read (pp. 159-161) that the good old rule may be set aside under no less than six contingencies. These contingencies are, of course, assumed to be the result of abnormal conditions, but we wonder uncomfortably what is the value of a rule that will not stand the test of abnormal times. Who will decide when times are normal or abnormal for any given trade? Lacking the powerful support of "the auditor's bible" (as it has been happily styled in the past), who can now successfully oppose the arguments of the client who insists upon higher market value for his inventory?

The author himself does not appear to be any too happy over the matter (see preface), and the reviewer thinks he will be even less so when future "heretics" quote Montgomery's *Auditing* against the "cost or market" rule. Protest and point as he may to the qualification that "unrealized profits . . . must be separately stated," the door is open

to unlimited juggling with inventory values, and always will be pleaded the excuse of abnormal conditions. True, they were, and still are, abnormal, but is that any more reason for varying the standard in the case of inventories than in the case, for instance, of cash, which a certain economist proposes to "value" on a sliding scale?

The reviewer has long entertained a heresy of his own on the subject of inventories, and since he is no longer in danger of orthodox damnation, he proposes to state it. Why should we not abandon the double standard of "cost or market" entirely, and rely upon cost alone? As a matter of fact, cost is the basis of all real profit in the end, allocate it as we may to different periods by the present rule of "cost or market." The argument that the balance-sheet should show the true financial position at a given date and therefore the inventory must be priced at cost or market, whichever is the lower, sounds plausible, but the reviewer thinks it fallacious in most cases. If the concern is about to go out of business, it would be correct, but no concern puts out a balance-sheet for any purpose whatsoever which does not intend to continue business as usual. It is, therefore, rather final to maintain that it should show its inventory at market price when it has no intention of selling at that price. On the other hand, by stating its inventory at cost (eliminating, of course, damaged and unsalable goods) it would be showing its true financial position for the reason that it would thereby show the amount of working capital invested in material or merchandise. As for the profit-and-loss statement, cost basis would show the actual cost of sales. In an abnormally rising selling market, this profit would naturally be abnormal too, but it would be offset by smaller profits when the concern had to replace material or goods at higher prices. Using the "cost or market" rule distributes or equalizes the real profits between two periods, and *it does nothing more*. The ultimate profit realized on the sale of a given lot of merchandise is the difference between the actual cost and the actual selling price realized. Why not frankly recognize the fact, which every merchant knows, and thus do away with a perennial cause of conflict between auditor and client?

As for presenting a balance-sheet that "may more nearly reflect a concern's actual financial position" (page v), would it not amply suffice to state the market value of the inventory as a note under "inventories"? We do that in the case of long-time investments, and the inventory reflects nothing more nor less than a temporary investment of working capital.

But to return to *Auditing*—Montgomery's work is too well known to need any commendation to the profession. The reviewer does wonder, however, what the accounting world will think of the chapters on inventories. Shall we agree that the author has treated the matter in the light of common-sense and expediency? Or must we admit that in this world of chaotic welter even accountancy has lost its standards? And how will it all end? W. H. LAWTON.

Book Reviews

APPLIED GRAPHOLOGY, by ALBERT J. SMITH. *The Gregg Publishing Company*, New York. 197 p.

There is so great a tendency to read meanings into meaningless facts that there is always a certain amount of doubt as to the value of any interpretive science. The world is full of people who believe in astrology, palmistry, clairvoyance and what not. This must be so because there are so many people engaged in imposing upon the public in these ways.

A quite valuable attempt to read character and faculty from handwriting has been the subject of a certain amount of skepticism because at first glance it seems to be somewhat like trying to foretell one's future by the horoscope.

The writer of these notes remembers clearly that in the halcyon days of reportorial irresponsibility he was called upon to take the place of the graphologist whose duty it was to classify and characterize letters which were sent in anonymously accompanied by a modest fee. The thing seemed so simple that it was undertaken gleefully. The first issue of the paper in which his expert opinions appeared described one correspondent as likely to be more at home peeling potatoes than handling a pen. It subsequently developed that the lady in question was one of the leaders of society of the city in which the paper was published. From that time onward all attempts at graphology have been left to those who know something about it.

Applied Graphology, a new textbook on the subject of character analysis from handwriting, is extremely interesting and seems to be well worthy of consideration. Accountants would probably get many a valuable hint as to conditions if they learned to read character from the handwriting before them

A. P. R.

PRACTICAL BANK OPERATION, prepared by L. H. LANGSTON.
Ronald Press Company, New York. 2 vols. 731 p.

These volumes were prepared under the direction of the educational committee of the National City Bank of New York primarily for the use of the bank's training classes and incidentally for the use of bankers and students in general. The work is strictly a practical manual describing in great detail how the affairs of a great banking institution with branches and connections extending throughout the civilized world are carried on. This means not only how the clerical details are taken care of in the bank itself, but also the travels and adventures of "items" which may go from the bank perhaps to the nearest clearing house, perhaps to London, Paris, Buenos Aires, Calcutta or the cities of far Cathay. It is rather stirring to the imagination to see what an important part bank credit plays in the world's affairs, and it helps one to understand better the chaos following the general collapse of that credit during and after the war.

With the possibilities of a large foreign trade being built up in this country before them, ambitious American manufacturers and traders will find much useful information as to handling the details of the necessary financial transactions, as well as the service banks with foreign connections can render in the way of investigating the credit and responsibility of

would-be foreign customers. The chapters on foreign collections, dis-accounts, exchange, etc., are full and enlightening.

The part played by clearing houses and the federal reserve system is fully explained and discussed, a matter on which there is need of much light in these days when attempts are being made to subject the federal reserve system to political control for the benefit of this or that bloc. Other functions of the modern bank are treated in the same detailed and exhaustive manner.

The public accountant will be chiefly interested in the chapters on credit and on the bank's methods of internal check and audit. From the casual remark (p. 244) as to the preference given by bankers to certified statements from would-be borrowers, it is apparent that the status of the public accountant is well settled among bankers. In return it would be only fair on the part of the accountant to give careful study to the points, as set forth in the chapter on credit, about which the banker desires explicit information.

W. H. LAWTON.

TRADE TESTS, by J. CROSBY CHAPMAN. *Henry Holt & Co.*, New York. 435 pp.

Naturally the title, *Trade Tests*, provokes at once the question, "What is a trade test?" The definition given by the author (p. 8) is—

"Essentially, the trade test is a measuring rod which can be used without trade knowledge on the part of the examiner, for rating in objective, quantitative terms the degree of trade ability possessed by the person under examination."

This gives us the subject and the object of the whole book—it is a study of methods of framing a set of questions adapted to the trade by which an examiner who has no special knowledge of that trade can ascertain with approximate accuracy, and express by a scale, what an applicant for a job actually knows about it, and how he should be ranked, whether as a novice, apprentice or journeyman-expert. Observe the significant points of this. The set of questions must be framed so it can be used by any intelligent clerk in the employment department instead of taking the more valuable time of an employer or foreman to question and experiment with the new man. The answers to the questions must be rated on an inflexible scale, no part credits being given: the applicant either knows or does not know. A pre-determined division of the scale automatically classes him as a novice, apprentice or journeyman-expert. Above all, the subjective element must be absolutely eliminated—the opinion of the examiner as influenced by the state of his digestion or by the personal appearance and manners of the applicant must have no weight in the final rating.

This is a large subject, and one may readily imagine the hoots of derision with which old-fashioned employers and foremen would greet this innovation. Luckily there are two factors in the author's favor: the lively tendency on the part of the up-and-going American employer to "try anything once," and the remarkable success of the tests used in the army during the late war. Although some attempts at such tests had already been made in a few large factories and

works, it was the enormous pressure of necessity during the war that put the adoption and use of these tests on a scientific basis. Millions of men had been gathered together in camps; thousands of them were urgently needed for technical jobs of all kinds, and the officers had to find them. Attracted by the prospects of extra pay and privileges, and above all by the laudable desire of many to get "over there" as soon as possible, hundreds of men professed ability and were accepted by confiding officers only to prove worthless for their particular jobs when they arrived in France. Of course, this meant waste and useless expense, and it became necessary to find some mechanical means of selecting and rating men for these technical positions. Dr. Chapman's book tells how it was done, including the not least valuable information to those who may attempt to adopt the methods hereafter: what errors were made, why and how they were corrected. Illustrations of standard test questions as finally adopted by the army authorities complete the story.

There are three methods—the oral test, which consists in bringing the candidate before the examiner who reads to him the set of questions drawn up for his trade and takes down his answers verbatim, the rating according to scale being done later; the picture test, in which the candidate is shown a set of trade pictures (tools, machinery, machine-parts, etc.), and asked their names and purpose; and the performance test, in which the equipment of tools and material for a standard trade job are given the candidate, and he is rated according to the time of performance and the quality of the product. In the oral and picture tests the questions are so framed as to require answers of but two or three words, but it will be observed that correct answers show trade knowledge and actual experience, thereby automatically classifying the applicant as a novice, apprentice or helper or journeyman or expert. The picture test is merely a variation of the oral and is used mainly where the applicant's knowledge of English is slight. Nevertheless, he may be an expert at his job and will be familiar with trade nomenclature. Both these tests are available, of course, only in trades where information is a large element. If the trade is almost purely a matter of dexterity, manifestly not much idea of a candidate's ability could be obtained through the question test. But in the case of a surveyor, bricklayer, electrician, etc., skill in carrying out processes follows almost automatically from possession of the necessary information he has acquired while learning them. Therefore, where manual dexterity is the chief element the performance test is indicated, but it may also be very useful in supplementing the oral and picture tests both to check the rating obtained by the latter and to ascertain the relative skill of several applicants for the same job.

In all cases the questions and performance tests are standardized by being tried on workmen of different classes. After correction and revision the examiner is not permitted to vary the language or form of the adopted questions when putting them to the candidate.

This insures impartial treatment and also the relative accuracy of the ratings.

And of what interest is all this to the public accountant? Well, the problem of excessive and wasteful labor turnover is an important subject for investigation when ways and means of cutting expenses are being sought. The right man on the right job means a contented man as a rule. Trade tests aim to establish this happy combination at the outset. They can also be readily adapted to ascertain the fitness of applicants for advancement. The public accountant who is familiar with Professor Chapman's book can be of great service to clients with long payrolls.

W. H. LAWTON.

R. A. O. A. 1921 SYNOPSIS, edited by E. R. WOODSON. *Railway Accounting Officers' Association*, 1116 Woodward building, Washington, D. C. 400 pp.

This is a synopsis of rules, regulations and forms for railway accounting as adopted by the Railway Accounting Officers' Association with the view of simplifying procedure and eventually establishing uniform methods in railway accounting. The book is divided into four principal sections: freight, passenger, disbursement and overcharge claim rules. The first three sections are further subdivided into mandatory and recommendatory rules; the last is entirely mandatory. Each section is prefaced by a complete index, and followed by standard forms to be used.

"Mandatory" is not to be taken in the sense that the rules are prescribed by the I. C. C. or other lawful authority. They apply to members of the association only as members and are not to be enforced where they conflict with state or federal laws or rulings.

The book is, of course, intended only for the railway accounting offices, but public accountants engaged in railway work, or even in auditing the accounts of large shippers, will do well to become familiar with it.

W. H. LAWTON.

RAILWAY ACCOUNTING OFFICERS' ASSOCIATION: THIRTY-SEVENTH REPORT. Issued by the *Association*, 1116 Woodward building, Washington, D. C. Cloth. 575 pp.

This is a report of the proceedings of the meeting of the Railway Accounting Officers' Association held at Atlantic City in June, 1921, and contains the usual addresses and committee reports customary in such bodies. To the accountant employed in or interested in railway accounting, the committee reports will be invaluable since they give the rulings and recommendations adopted for railway accounts in detail.

The general reader will be more interested in the addresses delivered by Commissioner B. H. Meyer, of the interstate commerce commission, and W. A. Colston, director of finance of the I. C. C. In these two addresses will be found illuminating information in regard to problems arising under the transportation act of 1920. From the general tenor of the remarks of Mr. Colston it is apparent

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that congress was no more successful in drafting the transportation act clearly and coherently than it was in the case of the income-tax laws.

W. H. LAWTON.

MUNICIPAL ACCOUNTS, by JOHN ALLCOCK. *Gee & Company*, London. 232 pp.

In the first ninety-seven pages of this compact little book (it is small enough to slip into an overcoat pocket) the author has accomplished the rather difficult task of outlining a complete set of accounts for an ordinary English municipality. The rest of the book contains all the forms for the accounts, reports, vouchers, etc., etc. According to the introduction (p. xii), the primary purpose of the book is to enable a borough treasurer, or the chief executive financial officer by whatever name known, to "give the maximum information" in as concise a form as possible to the members of the town council. It will be remembered that Mr. Oakey's book on state and municipal accounting, reviewed in these pages a short time ago, had the same object. Both serve a much more practical purpose in furnishing authoritative texts for the accountant, student and practising.

Owing to the similarity of municipal governments of this country to those of Great Britain, students who wish to acquire the fundamental elements of municipal accounting will find Mr. Allcock's little manual very helpful. Due regard, however, must be paid to differences in terminology and usage, e.g., "corporation redeemable stock" for municipal bonds, reversed debit and credit sides of accounts, etc.

W. H. LAWTON.

Marwick, Mitchell & Co. announce the opening of an office at 507 Main street, Worcester, Massachusetts.

John C. Stell announces the opening of an office at 280 Broadway, New York.

George E. Holmes, Ross W. Lynn, Randolph E. Paul and Valentine B. Havens announce the formation of a partnership, practising under the firm name of Holmes, Lynn, Paul & Havens, with offices at 15 William street, New York.

Charles L. Hughes announces the opening of offices at 110 William street, New York.

Lybrand, Ross Bros. & Montgomery announce that George Roscoe Keast has been admitted to membership in their firm in charge of their Pittsburgh office.

Arthur Young & Co. announce that A. O. Cushny has been admitted as a partner in association with Edward Fraser in the management of their office at 1105 Commerce building, Kansas City, Missouri.