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Federal Income-Tax Law and Regulations versus New York State Law and Regulations

By Eugene M. Travis

Notes on differences which must be borne in mind in the preparation of returns of personal incomes

The New York state income tax law is substantially the same in its provisions concerning the determination of income as the provisions of the federal law. The state income tax regulations were also made to agree with the similar federal regulations so far as possible. Nevertheless, there is a sufficient number of differences to keep the accountant alert and wary. These differences are referred to in this article. It is not the purpose of this article to discuss the merits of the respective differences but merely to call attention to them.

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Gross Income Defined: Inclusions

1. Personal service compensation.
   Compensation for services performed prior to January 1, 1919, is not taxable under the state law and regulations even though received in 1919. Under the federal law, it must be included in the return.

2. Salaries of government, state and municipal employees.
   The federal law exempts from tax the salaries of state and municipal employees, but taxes the salaries of federal employees, excepting that up to $3,500 of the compensation of persons in the
Federal and State Income Taxes

naval or military service is exempt. The state law provides that federal salaries are exempt from tax but taxes salaries paid by states and municipalities. "Municipalities" in both instances includes all political subdivisions of the state.

3. Interest income.

Interest earned or accrued prior to January 1, 1919, is not taxable under the state law and regulations even though received in 1919. Under the federal law, it must be included in the return. The state law exempts from taxation interest on bonds on which the investment tax was paid between June 1, 1917, and May 14, 1919, during the period of years for which such tax shall have been paid. Interest on these securities is, of course, taxed under the federal law.

4. Interest on government, state and municipal bonds.

The federal law exempts from taxation interest income from all state and municipal bonds and certain federal bonds. There are also partial and qualified exemptions on certain issues of Liberty bonds. The state law exempts in full interest from all federal bonds and obligations and those of the state of New York and municipalities of New York state but taxes the interest on bonds and obligations of other states and their municipalities.

5. Interest on tax-free-covenant bonds.

Taxpayers receiving interest on tax-free-covenant bonds are entitled to a credit against their tax of two per cent of the amount of interest, as the obligor corporation paid a tax of two per cent to the federal government. The state law does not provide for the payment of tax at the source by the corporation; so obviously there is no such credit allowed on the state return.

6. Dividends.

Dividends are exempt from the normal tax under the federal law. There is no such exemption under the state law, and all dividends are taxed in full.

Dividends received in 1919, which were declared payable to stockholders of record in 1918, are not taxable under the state regulations. They must be included in the federal return.
7. Stock dividends.

In the preparation of a federal return, the year in which the earnings distributed by the corporation were accrued is of significance in certain cases, but it is of no importance under the state law and regulations.

Stock dividends are taxed under the state law as they are under the federal law except that the federal law and regulations provide that they shall be returned as income in the amount of the earnings or profits distributed, usually equal to the par value of the stock distributed. Under the state law and regulations, stock dividends are income in the amount of the value of the stock received as a dividend.

It should be borne in mind also that the Macomber v. Eisner case is not controlling on the state, as the question of the right of the state to tax stock dividends, if raised at all, must be decided on different grounds than those which will control the decision under the federal tax law.

8. Personal service corporations.

The federal law classes personal service corporations with partnerships and taxes the stockholders of such corporations on their distributive share of the income of such corporations in the same manner as if they were members of a partnership. The state law has no such provision. Personal service corporations are not distinguished from other corporations. This leads to the following substantial differences:

(1) A personal service corporation must file a partnership return under the federal law, but is not required to file a return under the state income-tax law. [It is, however, obliged to file a return with the state tax commission under the corporation franchise tax law.]

(2) Stockholders will return to the federal government their distributive share, whether received or not, of the income of the corporation, but are not required to report that on the New York state return.

(3) Stockholders are not required to report dividends received from a personal service corporation on their federal return but are required to report such dividends on the state return.
Federal and State Income Taxes

GROSS INCOME DEFINED: BASIS FOR DETERMINING GAIN OR LOSS

9. Sales of property.

The federal law provides that in computing loss or gain from the sale or other disposition of property, the cost or value on March 1, 1913, if acquired prior thereto, must be taken as the basis. The state law provides that the basis is cost or value on January 1, 1919, if acquired prior to that date.


The federal regulations do not provide that any loss or gain results from the gift of property to others. The state regulations provide that a gift is an "other disposition" of property within the meaning of the statute. If one gives property to another, he suffers a loss or realizes a gain, depending upon whether or not the value of the property at the time of gift is greater or less than cost (or value on January 1, 1919, if acquired prior thereto).

DEDUCTIONS ALLOWED

II. Interest deductions.

The rules for the deduction of interest payments (or accruals) are different under the two laws. The federal rule is that all interest paid or accrued may be deducted except interest on indebtedness incurred or continued to purchase or carry securities, such as municipal bonds, the interest upon which is exempt from tax, the exception not applying to certain issues of Liberty bonds. The state rule is that the taxpayer may deduct that proportion of interest paid which his gross income (that is, income from sources taxable under the state law) bears to his total income.

12. Traveling expenses.

The definition of allowable traveling expenses is somewhat more liberal under the state law than under the federal law. The state regulations define allowable traveling expenses as including railroad fares, meals and lodging, if the trip is undertaken for business purposes. The federal regulations provide that meals and lodging even on business trips continue to be living expenses and are not deductible in computing net income.
13. **Deduction of New York state income tax.**

The amount of income tax paid to the state of New York is an allowable deduction on the federal return but not on the state return. [Note, however, that this deduction can not be claimed under the federal return, except in the year of payment, unless accrued on the books of the taxpayer].

14. **Replacement fund for losses.**

The provisions of federal articles 49-50 with respect to replacement fund for losses have no counterpart in the state regulations.

15. **Depreciation and depletion.**

The regulations under both laws are the same on this subject except that the value of property on January 1, 1919, instead of that on March 1, 1913, must be used as the basis for determining these deductions under the state law. Likewise, the discovery provision under the state law with respect to deductions for depletion refers to discovery on or after January 1, 1919, and not to discoveries on or after March 1, 1913, as is the case under the federal law.

16. **Amortization.**

The provisions of the federal law, section 214a (9) and federal articles 181-188 inclusive with respect to deductions for amortization of war plants and facilities have no counterpart in the state law or regulations.

17. **Charitable contributions.**

The definition of corporations and organizations, contributions to which are deductible, is substantially the same under both laws except that deductions are allowable under the New York law only if made to corporations and associations incorporated by or organized under the laws of the state of New York.

**Credits**

18. **Personal exemptions.**

The federal regulations provide that a taxpayer’s status on the last day of his taxable year determines his exemption for the year. The state regulations contain no such provision, as status at any
Federal and State Income Taxes

time during the year will justify a claim for exemption. For instance, if a taxpayer’s wife dies during the year, he will be entitled to a married person’s exemption of $2,000 under the state regulations, but only to the $1,000 exemption of a single person under the federal regulations.

19. Credit for income taxes paid by a nonresident.

The state law has a “reciprocity” provision by which residents of a state that imposes an income tax are entitled to a credit for taxes paid to the state of their residence on income earned in the state of New York. That provision of the law is of academic interest only at the present time, as the comptroller has not ruled that any state has the proper reciprocal provision which entitles its residents to this credit.

20. Credit for income taxes paid to foreign governments.

The federal law provides that a citizen of the United States is entitled to a credit against his tax of the amount of income taxes paid by him to a foreign government on income earned abroad. There is no such provision in the state law, nor are such income taxes allowable deductions under the state law.

Nonresidents


The state law taxes nonresidents and nonresident estates and trusts only on their income

(a) From property owned within the state of New York.
(b) From a business, trade, profession or occupation carried on within the state of New York.

It does not tax nonresidents on their income from annuities, interest and dividends unless they are part of the income of a business, etc., carried on within the state of New York. A nonresident’s state return may, therefore, be totally different from his federal return.

The state income tax regulations for nonresidents have to be studied in order to determine the taxability of a nonresident. If a nonresident derives income from a business, trade, profession or occupation that is carried on both within and without the state,
special attention must be paid to the articles of the regulations dealing with the apportioning of such income. For the convenience of taxpayers, lawyers and accountants a bulletin is being prepared containing the regulations affecting nonresidents.

RETURNs

22. Forms of returns for residents.

The federal government has two forms of returns:
(1) Form 1040a—for incomes of not more than $5,000.
(2) Form 1040—for incomes of over $5,000.

New York state has two forms of returns for residents, but they divide on entirely different bases, viz:
(1) Form 200—for individuals whose incomes are derived entirely from salaries, interest, dividends, partnerships, estates and trusts, regardless of the amount of net or gross income.
(2) Form 201—for individuals having other sources of income such as
   (a) Income from business or profession (except as a partner).
   (b) Income from rents and royalties.
   (c) Profits from the sale or exchange of stocks or bonds.
   (d) Profits from the sale or exchange of lands, buildings and other property regardless of the amount of net or gross income.

23. Forms of returns for nonresidents.

Two forms of returns are provided for nonresidents:
(1) Form 200a—for nonresidents whose income from sources within the state is derived entirely from salaries, partnerships, estates and trusts, regardless of the amount of gross or net income.
(2) Form 201a—for nonresidents having income from other sources within the state of New York such as
   (a) Income from business or profession (except as a partner).
   (b) Income from rents and royalties on property located within the state of New York.
Federal and State Income Taxes

(c) Profits from sale or exchange of lands, buildings or other property located within the state of New York.

Nonresidents who carry on business both within and without the state of New York are required to apportion their income; and the state income-tax regulations and the instructions on the forms of returns must be studied in the making of this apportionment. So also partnerships which (a) have a nonresident member and (b) carry on business both within and without the state and estates and trusts which (a) have a nonresident beneficiary and (b) carry on business both within and without the state must likewise apportion their income so as to exhibit the proportion earned from sources within the state of New York.

24. First fiscal year returns.

In the preparation of first returns under the state law for individuals with fiscal years, the return of income must be made for the completed fiscal year and prorated according to the number of months in the fiscal year in 1919 and the tax paid on such proportion. The personal exemption must be correspondingly apportioned. In most cases, the federal returns for those individuals will be full year returns; so that while the federal tax will be computed on the total income for the year, the state tax will be computed on only that portion of it earned in 1919.

25. Deducting and withholding at source.

The provisions of the state law on the subject of deducting and withholding have no counterpart in the federal law. Employers are required to deduct the tax from compensation for services rendered within the state of New York paid to employees, who

(a) receive $1,000 or more during the calendar year; and

(b) do not file a certificate showing residence within the state of New York.

26. Returns of information at source.

The regulations in regard to information at the source are substantially the same under both laws except that the state law requires no certificates of ownership with respect to payments of
interest on corporate bonds, but it does require returns of payments of interest on registered bonds. The state law does not require information slips for each member of a partnership and for each beneficiary of an estate or trust as is required under article 1073 of the federal regulations. The provisions of the federal law with respect to the return of information as to payments to nonresident aliens and with reference to foreign items have no counterpart in the state law or regulations; and, furthermore, the state regulations require no returns of information respecting payments to nonresidents of items which do not constitute taxable income under the state law.

27. *Due date for filing fiscal year returns.*

The federal law and regulations provide that fiscal year returns shall be filed on or before the fifteenth day of the third month following the close of the fiscal year. The state law contains no special provision with respect to fiscal year returns and the provision that returns shall be made on or before the fifteenth day of March of each year for the taxpayer's last preceding taxable year applies to fiscal year returns as well as to calendar year returns, so that a return for a fiscal year ending June 30, 1919, is not required to be filed until March 15, 1920, under the state law, although it must be filed before September 15, 1919, under the federal law.
Accounting for Food Preserving Companies*

BY RAYMOND E. BARTH

The manufacture of food products which are in the nature of delicacies rather than staples has assumed the proportion of one of the large industries in this country and concerns in this business have become well known throughout the world through well conducted sales campaigns and advertising. Every effort is made to protect the quality of the products by the companies themselves, through the employment of skilled chemists, and by the government, through the enactment of pure food laws. Yet little or nothing has been developed in the way of standardization of accounts and costs.

Such businesses are competitive in nature not only with other concerns in the same field but also with the public itself. The products manufactured consist of such foods as fruit preserves and jellies, condiments, such as ketchup, chili sauce, salad dressing, pickles, etc. These products are also preserved quite extensively by house-wives; and in order to sell their product advantageously, the manufacturers must produce and sell at a price which the public will pay for such articles. There are standard products, known mainly through their trade names, which are ever in demand. In meeting this demand, there seems to be no disposition on the part of the smaller manufacturers to employ accounting methods which will give them necessary data for sales campaigns. The plan with them seems to be rather to fix their selling prices to meet those of competitor companies.

In this treatise are discussed only those accounting features which appertain particularly to this class of industry, without covering in complete detail all the accounting requirements of these businesses. These peculiarities are commented upon in the succeeding paragraphs under the following main headings:

1. Raw materials.
2. Finished product.

*A thesis presented at the November, 1919, examinations of the American Institute of Accountants.
RAW MATERIALS

Purchases of materials are made from different sources, depending upon the size of the company. Many of the larger companies have farms on which they produce a large part of their raw materials. Others buy the raw product direct from the farmer under a system described later. Other smaller companies purchase raw material in various semi-finished forms. It is usually necessary for the larger companies to resort to all three of these methods to obtain raw materials. It is to the company which obtains materials from all sources that the following comments apply.

A company which has farms of its own, from which it obtains a large part of its raw product, must necessarily keep farm accounts in order to know the cost of materials grown and to ascertain the advantages or disadvantages of operating the farms as compared with other means of obtaining materials. These farm accounts are simple in nature and record the actual costs of all farming operations necessary to the production of the raw material. Accounts are kept for each farm; and where more than one raw product is grown on any single farm, it is necessary to sub-divide the costs of operation among the several classes of material produced on the basis of acreage. Cost of the resultant production is computed at the proportionate rate per unit of measure that the production units bear to the entire cost. At this point, comparative costs may be obtained between the raw materials grown on the several farms and raw materials purchased from outside farmers.

Contracts for materials purchased from farmers are ordinarily made during the winter and spring months. Through field agents in the different territories in which the necessary products are grown, the company contracts with the farmers for the output of a certain number of acres at a fixed rate per unit of measure of product. Products from farms are ordinarily received by the company at salting stations where the raw product undergoes the necessary preliminary treatment to preserve the quality until it
Accounting for Food Preserving Companies

is needed for further processes. This preliminary treatment usually involves storage in tanks with preservatives, such as salt brine, or possibly cutting, drying or some such operation. In the case of some materials it is necessary to boil the vegetables to a pulp and sterilize in cans until needed at a later date. The expenses at the salting house consist of the costs of the product purchased from the farmer, together with the necessary labor and expenses involved in preparing for storage and shipping to the factory. All expenses directly applicable to the individual products are charged direct to the materials produced, and expenses not directly applicable, such as superintendence and office expense, are usually apportioned on the basis of acreage purchased from the farmer. The total cost of each class of semi-finished material when through the salting house is divided over the total output of that product to obtain a unit cost at this stage. Comparison may then be made with raw materials purchased on the outside in a semi-finished stage.

Purchases of raw material in a semi-finished stage are ordinarily made from brokers or manufacturers handling materials at this stage of completion. The prices paid for this class of material are usually current market quotations which prevail among all buyers at the time.

Materials and supplies used in manufacturing the raw materials into finished goods are purchased in the usual manner.

Finished Product

The handling of costs of finished product is comparatively simple. The raw material at its purchase price or its known cost is charged into the operation developing the finished product. The labor and direct expense, including manufacturing, bottling, canning or storing, labeling and packing, are all direct costs to the finished product and the overhead is applied in accordance with the plan discussed under “distribution of overhead.” These costs are applied to the finished product in units of dozens except when barrels, pails or kegs are used as the unit. The total dozens produced in each run are divided into the total cost of each batch produced in order to obtain comparative costs for each run of production. However, for the purpose of monthly costs, the average cost of all production for the month is used.
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Certain classes of the product, however, require special consideration. Pickles, for example, in their raw state are purchased as cucumbers at certain rates per bushel, varying with the average size of the cucumbers, the smaller cucumbers costing considerably more than those of the larger size. These pickles are taken to the salting stations and made into salt stock by the use of salt brine until ready for further process.

As it is needed at the manufacturing plant, this salt stock is shipped in tank cars to the manufacturing plant, where it is unloaded into barrels and sorted into the various sizes of pickles, the size name indicating the number of pickles per barrel. After each day's sorting, there are reported to the cost department the number of barrels of salt stock used and the number of barrels of each size of pickles obtained during the day's sorting. At the end of each month these daily figures are summarized to show the total number of barrels of large and small salt stock used and the number of barrels of each standard size of pickles obtained in the sorting.

In order to apply the cost of salt stock in the original grades of large and small to the finished products with a greater variety of sizes and apportion this cost equitably on the relative values of each size it is necessary to use a scale which will record the differences in value of the sizes. This scale consists of arithmetical differentials based on the graded differences in market quotations for the various sizes of salt stock. When the numbers of barrels of assorted sizes have been obtained at the end of each month, this scale is used by multiplying the differential for each size of pickles by the number of barrels produced of that size and obtaining a product representing the total cost above the base cost. This product is subtracted from the total actual cost ascertained from the cost of salt stock used during the month plus labor and overhead and the base rate per barrel is obtained by dividing the remainder by the total number of barrels. To the base thus obtained are added the scale differentials in order to obtain an actual cost scale for the month.

The base-rate fluctuates from month to month, depending on whether the salt stock averages above or below normal sizes for the grade of salt stock used, and the variation in the bases computed for the output of certain farms, purchases or salting house
Accounting for Food Preserving Companies

products is a useful guide to comparative values of salt product from the viewpoint of grade.

Distribution of Overhead

Food production is a seasonable business, i.e., during certain months of the year production is limited only by the capacity of the plant and crop production, while during other seasons of the year the entire efforts of the business are centered upon selling campaigns. It will be seen that a condition like this will have a vital effect on the method of distributing overhead expense, taking into consideration the fact that a very large percentage of the overhead expense is fixed and does not fluctuate with production. Furthermore, elements such as the use of machinery in certain departments as compared with manual labor in other departments have a vital effect.

In order to establish a satisfactory basis for distribution, it is necessary that complete analyses of operations be obtainable for past years. These operations must be analyzed into factors such as productive labor by months and by departments; value of production of sales by months and by departments; distribution of expense so far as applicable to departments by months; and all other conditions which affect the operations of the plant. After obtaining such analyses for prior years, the next object is to establish a rate of overhead on direct labor or on production centers which during the whole of an operating period will take care of the actual accrued overhead for the year. These percentages at first will be somewhat arbitrary, but may be adjusted from time to time as conditions warrant. In such a method of distribution of overhead, there are certain months in the year in which the production is heavy which will bear a larger overhead than actually accrues in those months, but this condition will be offset during the less productive months by smaller distribution of overhead than actually accrues. If the percentages for each department have been worked out in a careful manner, there should be no great discrepancy between the actual overhead accrued during the year and the overhead distributed during the operating period. If there is a large discrepancy it will be due either to inaccuracy in the percentages used or to some unusual condition arising which was not covered in the percentage. In
one case the percentage of difference during the year was less than one-half of 1% of the total overhead for which provision had not been made.

**Inventory Control and Cost of Sales**

It is advisable, indeed essential, that a proper control of the inventory be obtained, but the very nature of the product makes it unusually difficult, owing to the fact that there are so many classes of product and so many small units. It would otherwise be impossible to place responsibility for shortages on any one person on account of the size of the stock and the number of people handling it and shipping it.

A satisfactory scheme is to have the loose stock piled in symmetrical piles, a certain number of units to a layer and a bin card or stock card used for recording the amounts placed in stock or taken out. The stock cards are controlled by a stock book. Reports of finished product are checked against the stock book, which in turn is checked against each stock card daily; and reports of withdrawals from stock are checked against the shipping orders and also against the stock cards daily. In turn, the withdrawals from stock are checked against actual sales by daily analyses of sales by quantity only. If loose stock is packed in boxes or cases, a separate stock record is kept for the cases and the piles of cases are checked daily in the same manner as are the loose piles. In this way it is possible to keep accurate control of the stock at all times both as a check against production reports and as a check upon cost of sales.

At the end of each month, the total production in units and money for the month is entered on a summary card. The units of sales are summarized and entered on this card. The unit cost of sales for the month is obtained by averaging the inventory at the end of the preceding month with the production for the month, the cost obtained being applied to shipments and the cost of sales thus ascertained. This cost is summarized by departments and a cost statement is prepared for the general accounting department showing the necessary data to be entered on the general records and also for the purpose of preparing financial operating statements.
Financial Records

Financial records differ only slightly from those of other manufacturing companies, with the exception that there must be some means of keeping in touch with the expenditures for raw materials at the different salting stations. Funds are usually provided for the men in charge of the stations for the payment for materials on delivery. They in turn furnish weekly reports to the company showing the expenditures and the purpose of such expenditures and these statements become part of the financial records and are handled in somewhat the same manner as are disbursements from petty cash funds.

Owing to the seasonable nature of the business, there are certain periods of the year when usually large sums of money are required, and, in order to obtain the necessary credit or financial assistance, it is imperative that the company be able to render a satisfactory form of balance-sheet based on actual figures. The preparation of such a statement would be impossible with any degree of accuracy unless some form of perpetual inventory were in use, because an actual inventory in a business of this character requires suspension of operations for an unusually long period.

Adequate Accounting a Real Necessity

The sales department in a business of this kind is usually larger proportionately than in other industries. The department must be organized and directed in regular selling campaigns along the most advantageous and profitable lines. While the disposition of the smaller manufacturer in this business is usually to fix selling prices to meet or undersell his larger competitor without even a fair estimate of his own cost to manufacture, few classes of business can be pointed out in which this practice is more dangerous. A manufacturer's large competitor usually grows his own crops and in cases of over-supply reduces his selling prices so as to move the product finished from such over-supply before the period of spoilage begins. The manufacturer who has only the competitors' prices to guide him has often been known to regard himself as successful on account of a large business in sales, when as a matter of fact he has been buying semi-finished product or raw materials in the market and finishing them at a cost greater than the well-organized competitor's selling prices.
Greenhouse Accounting *

BY A. F. WAGNER

Greenhouses are, in general, operated for growing either cut and potted flowers or market garden produce. These two types of greenhouses present many analogous problems, but it is intended that this article shall cover only the accounting requirements and peculiarities of the producing florist’s greenhouse. Furthermore, the retail distribution of the greenhouse product will not be considered, for the retail florist’s business presents only those accounting problems usually connected with the merchandising of highly perishable goods to customers who, at least partly, are poor credit risks.

The average floral greenhouse in its accounting aspects presents a peculiar mixture of a farm, an industrial manufacturing plant and wholesale merchandising. The last of these phases demands that most sales be made for cash or a sufficient reserve be set up for bad debts. Except for certain local holidays or festivals which stimulate the sale of flowers, the main selling seasons of greenhouses are Christmas and Easter, the sales for the two months in which these holidays occur often being more than double the volume of sales for the other ten months of the year. Owing to the outdoor growth of flowers in private gardens, the summer is by far the poorest selling season.

In spite of the seasonal nature of the business, there is no time during the year when the floral greenhouse is not producing some sort of a crop in expectation of a future selling season. Were it not for this constant production, a greenhouse could end its fiscal year on the date when no plants were growing, thereby securing a correctly priced inventory and a correct statement for the fiscal period.

We now come to the main difficulty in securing an accurate statement of annual profits and net income; namely, the proper pricing of the inventory of growing plants. The farmer usually

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has all his crops harvested at one season of the year, and can at least price the unsold portion thereof by deducting a percentage from the average market price prevailing for the previous few months. The greenhouse operator, always having some crop growing or "in process," can resort to no such methods, and often inventories growing plants by actually listing the cost of the seeds, bulbs, pots, etc., and making a guess at the cost of the labor and heat which have been expended on unsold plants.

From the above remarks it is evident that no greenhouse can be certain of its annual profits, to say nothing of knowing which crops are or are not profitable, unless its accounting system automatically provides a real inventory of growing plants (work-in-process) at cost. To accomplish this desideratum, it is imperative that the greenhouse accounting comprehend a cost system which is in many ways analogous to similar systems operated by manufacturers. The remainder of this paper will consider the ends to be accomplished by such a system, and, without presenting detailed forms, will endeavor to set forth some of the means of accomplishing these ends.

The advantages of having the cost records "tied up" with the general books need not be elaborated here, for it is sufficient to state that this should be done. However, before proceeding with the planning of any such system, an accurate plan should be made of the greenhouses showing particularly the number of square feet of floor space in each separate unit and, if the buildings are of various heights, the number of cubic feet in each house. Furthermore, the floor space of each structure should be divided into numbered "production plats." After this has been accomplished, no production should commence except when so directed by an order issued in the main office. Each production order should be issued for but one kind of plant or flower and should specify the kind of flower, the number to be planted, the approximate date when production is to be completed, the materials to be used and the house and plat number or numbers of the space to be used in the growth of the particular order. A duplicate of this order can be made to serve as a material requisition. In order that workmen may know at all times the production order numbers of each plat, such numbers, in large type, should be hung above the growing plants. The principal items of the cost
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of producing flowers arranged in the order of their usual importance are as follows: labor; heat; bulbs, seeds and shoots; building repairs. Therefore, in determining greenhouse costs, these items, in particular, must be carefully allocated to specific production.

In order that an accurate record of materials used in production and on hand may be obtained, perpetual inventory accounts should be operated under the following main headings: (1) bulbs, seeds and shoots, (2) pots, (3) soil and (4) fertilizers. The operation of the first two of these accounts offers no particular problem. However, the soil account should be segregated into raw soil and fertilized soil. If the raw soil is purchased, its cost per cubic unit is definitely known; but, if dug on the greenhouse premises, a record must be kept of the labor cost of digging and the cubic units dug. When fertilizer is added to soil, a definite amount of earth should be fertilized and thereafter kept on a stock pile separate from the raw soil, the cost of the fertilizer being added to the unit price at which such prepared soil will be charged to production. Because a greenhouse usually sells its product in two forms—namely, cut flowers and potted plants—it will be necessary to keep a record of all pots and soil remaining on hand at the completion of each production order. The unbroken pots should be returned to stock and credited to the cost of the production order at their cost price, and the remaining soil should be returned to raw soil stock and deducted from the production order cost at the average cost of raw soil. This latter price may vary somewhat from the original cost of the raw soil, but such fluctuations will be inconsequential in their total amount.

Direct labor is usually the largest single item in greenhouse production costs and consequently an accurate accounting for the time of all workmen is essential. Each employee should be provided with a daily time card on which he shows all orders on which he has worked and all operations performed during the day, whether they be setting out pots, planting, pruning, watering, cutting, or indirect labor, such as whitewashing or repairing glass. A large greenhouse is spread out over so much territory, and has so few workmen per square foot, that it is impossible for the superintendent constantly to observe the work of all em-
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employees. Consequently a certain amount of time should be spent daily examining employees' time cards in order to determine whether or not any employees are wasting time.

In designing a payroll book for a greenhouse, it is advisable to arrange the book so that the total direct and indirect labor, both hours and cost, shown on time cards may be proved with the total of each periodical payroll. Some greenhouses specialize so as to have only a few large production orders in process at any one time, in which case the payroll book may be drawn up so as to provide an analysis of direct labor by production orders. The employees in a greenhouse usually have little clerical training; hence all labor records which they are to make should be made as simple and easily understood as possible. However, with proper instruction of employees and with order numbers conspicuously displayed over every production plat, no great difficulty should be experienced in securing an accurate record of labor. In all cases, the actual hours of direct labor expended on each order should be shown on the cost sheets, for such hours are perhaps the best method of apportioning certain indirect expenses.

The indirect production costs in a greenhouse fall naturally into two main classes: the first consisting of heat and building expenses, that is, building services and rent or payments in lieu of rent, such as repairs, depreciation, building insurance and real estate taxes; and the second consisting mainly of superintendence and such indirect labor as does not constitute a building service. Apparently the most equitable way of distributing the first of these two classes is on the basis of square feet occupied by each order, or, in greenhouses of varying heights, on the basis of cubic feet. The incidence of the second class to production is most nearly in accordance with the direct labor hours; however, in some cases both classes of indirect production costs may be equitably distributed to production orders on the square foot basis. When this latter method can be adopted it recommends itself because of simplicity.

Greenhouses often have their main fuel stock in a pile outside the boiler room and maintain an approximate one-day supply in the boiler room. When this is the case, it is fairly simple to keep a record of amounts removed from the main stock and thereby determine a nearly accurate monthly fuel cost. When
this procedure is not followed, other means of recording the quantity and cost of fuel consumed must be devised. In order to determine a correct heating cost, all labor and expense connected with the boiler room or steam plant, including depreciation, should be charged as a heating expense.

Owing to the peculiar construction of a greenhouse, the fixing of a fair depreciation rate is a difficult problem. The glass roof and sides (which form a far larger part of the cost of a greenhouse than do the base and frame) are constantly being replaced. On first thought, it seems logical that the depreciation rate cover only the cost of the frame and base, the repair and replacement of the glass keeping the roof and sides in as good condition as when new. However, there's a rub, for, when it becomes necessary to replace a base and frame, approximately one-half of the glass is broken before it reaches its place on the new frame. Consequently the greenhouse has, roughly, a fifty per cent salvage value in the glass which has been kept in perfect condition at a heavy expense.

The indirect production costs or manufacturing burden of a greenhouse, except repairs, are not given to violent fluctuations but do fluctuate generally with the volume of production. It is, therefore, advisable that the actual manufacturing burden be charged into production orders as incurred from month to month. In order to level the monthly charges for repairs which are generally made during the summer, it is preferable to charge an estimated amount into the manufacturing burden each month and set up reserves for repairs against which the cost of repairs actually made can be charged. If this procedure is followed and all burden is charged to production month by month, there will be no large amount standing on the books at the end of the year representing manufacturing burden over-absorbed or under-absorbed. It is necessary to make annual adjustments for inaccuracies in the original estimates of steam plant and building repairs, but careful planning will reduce such discrepancies to a minimum.

In order to summarize the costs of individual orders, it is necessary to operate a cost ledger and cost sheets in a manner similar to the procedure followed in the cost systems of manufacturers. These cost sheets representing orders-in-process
should be controlled by a general ledger account, which may be styled "growing plants." Inasmuch as the plants are constantly growing and blossoming until sold or the end of their life, it is impossible to operate any account similar to the manufacturer's account "finished goods." Production in a greenhouse can usually be planned so as to be complete and sold in any one month. When an order reaches this completed state it should be removed from "growing plants" and charged to cost of goods sold. However, cases often arise when prematurely developed plants or flowers are sold long in advance of the final completion of the entire production order. Until the order is completed and sold such sales may be credited to a suspense account such as "invoices rendered on uncompleted orders" and transferred to sales when the cost of production is brought into cost of goods sold. Before finally determining the cost of a specific production, care must be exercised to see that all remaining usable materials have been returned to the proper stock accounts and deducted from the production costs shown on the cost sheets.

If efficiently managed, the selling and administrative expenses of a producing greenhouse should form a small portion of the total expense. For that reason, it does not seem advisable to undertake the clerical work necessary to allocate such expenses to each sale or group of sales. The chief executive, if awake to his position, knows the average percentages of these classes of expense, and can apply such percentages to any order when he so desires. Such expenses will appear separately in the monthly statement of profit or loss, and percentage calculations of these expenses also should be shown on that statement. This method therefore includes only actual manufacturing burden on the various cost sheets, which means that the cost figures must be combined with brains when they are used to determine a selling price.

The foregoing is a sketch of the main points to be considered in devising an accounting system for a floral greenhouse. If properly operated, such a system will not only afford an accurate statement of net income or loss for each fiscal period, but it will also present means of reducing waste of labor and materials and, further, give accurate data as to which are the profitable crops.
Uniform Accounting in the Textile Industry*

By Chester R. Union

A prominent man in the textile industry while discussing the development of the use of standard accounting methods asked: "Why should we capitalize all additions to plant and equipment? We have always charged them to expenses in order that the book values of the property might be conservatively stated." The idea is typical of many old and successful textile firms, that is, to use arbitrary accounting methods to establish hidden reserves in their financial statements.

The real objection to the use of such methods is not due to the purpose intended to be accomplished, but to the manner in which it is carried out. Perhaps the best answer would be a plea for the use of uniform accounting in the industry.

The use of uniform or standard accounting methods has been developed greatly during the last few years. Their advantages have been conceded in the case of accounting for public institutions, and they have been successfully used by all public utility industries. Several semi-public and private industries have more recently adopted generally uniform methods. The federal government, through its recent requirements for taxation, to some extent, has standardized accounting in all industries.

The textile industry, embracing the manufacture of cotton, woolen, worsted and kindred goods, is one of the oldest and largest of our industries. Many of the firms have been using about the same general accounting systems for a generation or more without embodying modern standard principles. As they have been successful financially and are large and powerful, it might be more difficult to convince these members of the industry that standard and uniform accounting methods for the industry would be a great improvement.

Uniform accounting for the industry might be limited to uniformity as to the accounting principles used and the requirement of certain results to be obtained through a uniform general

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classification of accounts and not necessarily be extended to any prescribed system or methods. The results required would be uniform financial statements which might follow the lines suggested by the federal trade commission as standard forms for general use. Simple uniform cost accounting systems could be adopted by the different branches of the industry which might be perfected by combining the best ideas in the industry and allow for extension according to the details desired.

The general advantages to be derived from uniform accounting by the textile industry may be grouped under three general divisions: (1) more general use of standard accounting principles and methods; (2) benefits from trustworthy comparisons; (3) general use as a basis for determining selling prices.

As the uniform accounting would embody the best accounting in the industry it would improve the methods of any firms which still used the old so-called conservative but inaccurate and misleading accounting methods. Uniform accounting means the use of standard accounting methods such as will show the true profits, expenses and financial condition.

If it were desired to reserve part of the profits to take care of unforeseen but possible losses, this would be done with the full knowledge of the directors and with a complete record thereof. The accounts kept to show the cost of the plant, for example, would show it correctly and be available for other uses, such as making the correct annual provision for depreciation; using the true invested capital in computing excess profits taxes; adjustment of losses from fires; in case of sales of the property; or showing more correctly the actual surplus of the company in case of sales of the capital stock.

The arbitrary methods common among many textile firms have resulted at times in concealing profits and understating the assets. Plant values have been reduced arbitrarily and concealed in reductions of the profits. Profits have been understated by including the cost of additions to the plant in the repairs, labor and materials expenses. Inventories of the product have been undervalued, causing misstatements of the profits.

These arbitrary charges to profits have occurred irregularly and only in years when good profits have been shown. In other years perhaps the proper provision for depreciation was not
made. The result might be that over a period of years good profits would appear to have been earned consistently each year. In this way the extent of the effect of the fluctuating conditions in the industry might have been concealed from the directors as well as the stockholders.

It is important, for example, that the directors be fully informed as to the effects of fluctuations in prices of the raw materials used. The importance of the policy of keeping purchases of raw materials covered by sales orders of the finished product will then be understood.

There was a common method, used by the cotton mills in New England, of understating the cost value of inventories of work in process. The materials in process of manufacture were valued at an amount far below the cost of the raw material, not to mention the labor and overhead costs. There was no system in the method except to make the value low for conservative purposes in financial statements. Usually the method was applied more or less to the finished product, resulting in understating its value also.

The common argument in the industry in defense of the method has been that if the plant were to shut down at any time the work in process would be worth only a scrap value. If the scrap value basis had been used consistently there would have been more merit in the argument. The values, however, varied from year to year without relation to the scrap values and when the method was applied to the finished product there was not the same justification for it.

It is impossible to find the profits on an accurate cost basis by using this method of valuing inventories. If it is desired to create a reserve out of profits, one may be established after the correct profits for the period have been shown.

A standard cost or market value basis of valuing inventories is now demanded for the purpose of determining the profits for taxation under the federal income and excess profits taxes. It should be noted that the additional value of the inventories on this basis increases the invested capital and therefore decreases the excess profits taxes to be paid. The requirements of the federal government through the income and excess profits taxes have made it necessary for the executives at least to take into
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consideration the results of these arbitrary methods. While many have believed it the easiest course to change their methods, they have done so as though compelled by the tax authorities. If they realized, however, the full significance of the indirect effect of their methods on their business they would have changed more willingly.

Capital stock is often held by trustees for the benefit of widows and children. They are entitled to know the exact condition of the business in order to determine whether to hold the stock or to sell it and replace it with an investment in a more stable industry, or perhaps to change from common stock to preferred stock or bonds of the same company.

If, in enlarging the business, additional capital were desired the bankers would require financial statements of the business covering several years. They would want to know the true financial position and the correct results of the business each year. The bankers, while appreciating the company’s explanation that its reports were conservative for one reason or another, would put more faith in the reports themselves and not have to rely so much on the character of the officers making them or on accountants if the reports were free from concealed arbitrary methods and were prepared on recognized, sound accounting principles.

Many textile firms have modern accounting systems and know their value. These firms, therefore, would be the quickest to see the additional advantages from uniform accounting methods in the industry. Everyone knows the value of the standard form of railroad reports for comparative and other purposes to the officers, investors and public. The principle of the standard form has many well-known advantages. The application to any particular industry or group will vary only in the extent of the details. The volume of details required in railroading, of course, would not apply to the textile industry.

The Harvard graduate school of business administration has undertaken to develop the use of uniform accounting in the retail shoe business. It is intended, also, as an example to other industries to show the advantages to be derived from the adoption of standard methods in general. Large numbers of firms have adopted it and furnish their statements periodically, from
which average statistics are prepared for their information and use.

In the interest of uniformity in balance-sheets and income statements, principally for industrials, the federal reserve board has published a pamphlet intended to standardize the form and preparation of these statements. This uniform standard of financial statements might be adopted as a general standard by any industry. The federal trade commission has seen the wisdom of recommending a simple and general cost accounting system for manufacturers in order to benefit those having only imperfect systems and by spreading this information generally to improve and more or less to standardize accounting methods. Another pamphlet was issued outlining a simple set of accounts for retail merchants.

One of the branches of the textile industry adopted a uniform cost accounting system within the past few years in an effort to educate the members of the trade to know their costs. A firm of accountants collaborated with members of the association and a simple uniform system was perfected which was adopted formally by the association and is used by a large number in the business.

When the form is accepted as a standard in the industry there will be a better general understanding and appreciation of financial and statistical statements. When it is known that certain firms' statements are inaccurate for one reason or another or are made up on an antiquated basis giving little opportunity for intelligent comparisons, the comparative value of the accounting statements of the industry is lost. A standard form would be simple to learn and understand; investors, bankers and officers would be more interested thereby; and the statements would be of much greater value to all.

Standard or accepted forms of statements would be useful for comparative purposes by officers. Different departments or mills in which they are interested might be put on an accurate comparative and competitive basis with each other. The causes of the weakness or strength in each might be graphically and quickly brought to the attention of the executives. A continuous record of the changes from period to period in these vital points of the business would give the proper guidance to executive
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judgment in operating the business. This, however, cannot be realized, unless the accounts and statistics are prepared on the same general basis and in the same form.

Comparisons are often made without preparing the accounts in this way and erroneous conclusions are necessarily reached. For example, waste from raw material, which is an important item in textile manufacturing, may be recorded in the accounts as an income or sale; it may be credited to the cost of the raw material when charged to process; it may be carried at the selling prices or at arbitrary percentages of cost prices. Loss on seconds may be shown separately, and on the basis of costs or on arbitrary basis are not to be shown separately. Labor may be carried in one account or may be subdivided into repairs and general mill overhead expenses, etc. Coal used may be charged on the actual weights or on arbitrary estimated weights with comparatively large adjustments when the stock on hand is verified. There may be differences as to where the line between plant replacements and repairs is drawn, leading to important differences in the amount shown as repairs expense. The mill overhead may be apportioned over the departments in one case and may be carried in lump sums in another or it may be apportioned on an incorrect basis. There are numerous ways in which differences in the preparation of statistics in the same business may be entirely misleading for comparisons.

In the case of comparisons between the results of different lines of business within the textile industry, only certain points of similarity are open to a beneficial comparison. However, from the financial point of view, valuable comparisons may be made as tending to show the trend of change between the kinds of business. The general percentage of profits on sales and on the capital as compared with previous periods is useful to the financial interests. Comparisons of the increase in volume of sales and increase in capital required are useful for different kinds of business to indicate where developments and enlarged operations should be undertaken.

Let us suppose that the same executives managing different lines of business in the textile industry have the accounts of these plants thoroughly examined and comparisons made. The comparative costs per unit for direct labor, material and over-
head for the different plants at the same date would not have much value. There might, however, be some value in statistics showing the comparative fluctuations from period to period as indicating the tendencies of changes. For example, it would be valuable to the executives to know the comparative increases or decreases in the various items of cost in the different lines of business, such as labor and materials, and also the comparative fluctuations in the margin of profits.

While one plant might have reported fair profits and perhaps in some respects have been arbitrarily conservative, yet with its reports completely prepared on the basis adopted by the others it might be found that this plant was not making a proper return on its investment. It is difficult to overestimate the value to the executives if this were found during a period when selling prices in general were advancing and might be fixed at any level within reason.

An example of the use of uniform accounting was seen in the federal trade commission's general investigation of cotton mill costs for the purpose of fixing maximum prices during the war. Costs and other data were prepared under a generally uniform system from the accounts and records of numerous mills. These were compared and averages were worked out. From this information maximum prices could be established intelligently at levels which would result in good profits to all.

Similar methods were used by the United States navy during the war in determining settlements for special articles furnished when prices could not be fixed in advance of production. The costs and other data were assembled under a generally uniform system. The results of similar firms were compared. These results could be used in making settlements which allowed good profits. Without this uniform system the purpose of the plan could not have been carried out.

The fundamental principle of the cost-plus contract is that to the measure of profit is to be added reimbursement for costs determined on standard cost accounting principles. The emergency contracts used by the government departments called for the use of accepted cost accounting principles applied uniformly in making settlements under the contracts.

It is evident that there are well defined and accepted general
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and cost accounting principles. If in the application of these principles to the industry the accounts are prepared under a uniform general classification, the results may be used for comparisons, which will form a sound basis for executive judgment in controlling the business.

Selling price levels can also be fixed by executives with approximate knowledge of the profit to be derived from their mills. If costs prepared by different mills are used as the basis for selling prices, the methods of preparing the costs should be uniform, or the executives will be relying on certain profits as being earned when in reality some mills may be losing money.

There are probably few cost accounting systems in use in the textile industry in general. In some instances, it may be considered that the business is simple and that costs may be readily ascertained by the use of estimates. This is perhaps true in a few cases but it would be easier to adopt a uniform system which has been accepted in general. In other cases of more complicated manufacturing, the actual costs are not known.

Both inadequate costs systems and lack of uniformity in calculating costs have been the cause of ruinous price-cutting. The industry should not be at the mercy of firms which do not know their own costs.

It would be the purpose of uniform cost accounting in the industry to prevent cut-throat competition. With the use of uniform cost accounting, there would be general appreciation of actual costs. If any companies chose to use price-cutting methods, they would fall with full knowledge of their costs and expectation of their doom.

It has been held that general trade organizations for the control and fixing of prices in an industry are illegal. If an association were conducted with the purpose of promoting better general knowledge of accurate costs as a basis for selling prices, the undertaking would have legal sanction as well as merit from a practical and business point of view. It would be to the best interests of the industry to establish the custom of basing selling prices on actual cost, plus a certain return on the investment.

Mill cost generally means the cost of the finished product in the mill. In addition the executive must consider the general administrative and selling expenses, plus the profit, in determin-
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ing minimum selling prices. The general overhead is almost uniformly expressed in the form of a percentage of the expenses to the mill cost, usually taking into consideration the volume of business for the period. There are also general principles to be observed in application of the profit allowance to costs for determining the minimum selling price basis.

For example, suppose a twenty per cent return per annum be considered a necessary average margin of profit in the textile industry. As a general proposition, the average total assets used in the business, less the non-interest-bearing liabilities, represent the capital entitled to its return. The volume of business at the mill cost plus general overhead expenses constitutes the turnover, which may be expressed in its percentage to the capital. If the turnover be at the rate of once a year on the capital, the rate (twenty per cent) which is to be earned on the capital, may be applied to the cost, plus the general overhead, for the profit allowance. If the turnover be twice a year, one-half the rate of profit or ten per cent may be applied to the cost and yield the same rate or twenty per cent per annum on the capital.

The necessary return on the capital may be calculated more closely by including in the profit allowance only the specified rate of return on any capital in the form of interest bearing indebtedness or preferred stock. The result would be that with a smaller total profit allowance the same rate of twenty per cent might still be earned on the common stock. If the product is divided into different classes which utilize entirely disproportionate amounts of capital, the latter should be sub-divided between the departments in determining the capital on which the return is to be completed.

The value of uniform accounting to the textile industry in educating its members to know their costs and necessary margin of profit in order to prevent unintelligent competition alone would be sufficient to make it desirable. The other advantages, however, are equally important in providing accurate comparative statistics for the guidance of executive judgment, in improving certain antiquated methods used and in increasing intelligent use of financial reports by bankers and investors which would serve to put the industry in its proper light.
Accounting in the Peanut Industry*

By W. S. Taylor

As an industry the cultivation and production of the humble peanut has in recent years reached such proportions as to astonish most of those not directly connected with it in a commercial way.

The peanut is essentially a product of the south and is most largely cultivated in the states of Virginia, North Carolina, Alabama, Oklahoma and Texas, with Alabama in the lead as to volume of production. It ranges in size and quality from the small, round Spanish to the enormous “Jumbo.” The sale is, to the mind of the uninitiated, consummated through the channels of trade represented by the automatic selling devices, the corner peanut vendor with his portable roaster (invariably equipped with a steam whistle) and the quite as popular peanut butter.

The crop matures in the states of Virginia and North Carolina about the first of October and is harvested by plowing. The vines with the nuts clinging to them are then piled loosely around stakes in the field for the necessary process of drying, after which they are put through a unique and very capable machine similar to a threshing machine, run by a gasoline engine and called a peanut picker, which most thoroughly separates the vines and nuts which are then placed in sacks for market.

The producer is primarily dependent upon the cleaner and sheller (whose establishment is known as a factory) for his market, and the latter is usually located in close proximity to the producing sections.

Buyers representing the cleaners and shellers are the usual medium through which original sales are made. They are salaried employees, commission men or free lances who take the chances of the fluctuations of the market.

The crop is almost invariably bought for cash. If shipped by rail, sight draft accompanied by bill of lading is the usual

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method of settlement, while what are termed "door purchases," i.e., deliveries by team or motor truck to the factory, are paid for immediately at the factory office.

The sight draft purchases are of course handled through banks in the usual way. Door purchases in the factories which the writer has in mind are checked for weight and quality by a superintendent or foreman who issues to the seller a receipt carrying weight and price, which he presents for payment to a cashier, who in turn, at the end of each day, reports to the general office the amount of the purchases, attaching the receipts as evidence of the acquisition of the commodity for which payment has been made.

By arrangement with the banks, cashiers' cheques are drawn for these purchases, which are treated by the banks as sight drafts and as such are presented in the usual way to the general office of the factory to be taken up by cheque.

In both instances the payments become a charge to "peanut purchases," and the entry carries a memorandum of the number of bags.

The cleaning and shelling process is of course largely mechanical, such peanuts as are to be sold in the shell being treated to a polishing process into which enters the use of a fine gritty powder known to the trade as "cleaning product." This gives the peanuts an attractive appearance with a velvety surface and a suspicion of a powder similar to talcum which naturally disappears in the process of roasting.

With the exception of the sorters the employees are carried upon the regulation payroll. The sorters are usually negro women and children who are paid for piece work by brass checks redeemable once a week at the cashier's office and in some instances, by agreement, are accepted by merchants in lieu of cash and redeemed by the cashier at stated intervals.

The sorters are closely seated on either side of slowly moving belts on which the peanuts drop from the cleaning machines and certain sorters remove designated sizes as they pass. A foreman in charge of each gang furnishes each worker with a card on which denominations are printed conforming with and in multiples of the piece work price, on which as the work progresses he punches the accumulation. At the end of the day these
cards are exchanged for brass checks equaling the largest amount or amounts punched.

The method of handling the brass checks is as follows:

All purchases of brass checks, which are in denominations of 5, 10, 25 and 50 cents and $1.00, are charged in volume and at denomination values to a memorandum brass check account and are in the custody of the general office.

Requisitions in triplicate are issued by the factory superintendents, the original and duplicate being sent to the general office and the triplicate retained.

These requisitions are honored by the general office by the issuance of brass checks in the denominations desired, retaining the original and delivering the checks with the duplicate to the cashier, who, after verifying the count, records the volume and value, in a record provided for this purpose, and delivers them to the superintendent, who again verifies the count.

These checks are issued by a foreman to the workers at the end of each day and are presented by them to the cashier on a regular pay day for redemption or are used by them in trade with merchants.

On the morning of pay day the cashier notifies the general office of his cash needs for brass check redemption, accompanying his request with the duplicate requisitions. These are checked against the original requisitions and a check covering the required amount is issued and cashed for payroll purposes.

All brass checks cashed by the cashier are credited upon his record and the balance shown as outstanding should equal his cash balance.

The checks are then turned in to the general office, receipt is given to the cashier for their volume and value, and they are charged against the general office brass check account, the balance outstanding representing the amount of cash that should be in the hands of the cashier, the correctness of which is verified at irregular intervals.

In some circumstances the punched cards are presented to the cashier by the worker to be exchanged for brass checks. This necessitates the keeping of a record of cards thus redeemed for payroll purposes and the issuance of requisitions in duplicate to the general office.

One feature of the business which tends to simplify the
accounting work is that settlement of customers' accounts can be required by invoice or invoices. Several factories that have come under my notice do require such payments.

This condition permits the elimination of the usual subsidiary accounts receivable ledger which requires the posting of all invoices and settlement items, such as cash, discounts, rebates, allowances, freight adjustments, etc., by the adoption of the following method:

Invoices are made in triplicate (unless the customer requires two or more copies) and are numbered consecutively.

The original goes to the customer with bill of lading.

The duplicate and triplicate invoices, which are perhaps an inch or two wider than the original (but all are of the same depth), are punched to fit binders and are provided with printed forms for recording date and nature of correspondence, such as request for payment or discussion of claims, as well as for the recording of the details of settlement.

The duplicate is filed daily in an indexed binder which becomes the account receivable ledger, invoices to each customer being grouped, with the one of the earliest date appearing first in each group.

As settlements arrive the proper entries are made in a cash journal and posted to the invoice or invoices included in the settlement. Such invoices are then removed to a transfer or paid accounts receivable binder, similarly indexed, for future reference.

As these transfer binders fill up they are marked on the binding end with the payment dates which they cover and are filed in consecutive order on shelves usually provided in the office vault.

The triplicate invoices are filed numerically in a separate binder and become records of sales, which are accumulated monthly, by adding machine, upon plain sheets, similar in size and punching—but of a distinct color—and the total of bags and value is recorded in a cash journal to the debit of accounts receivable control account and to the credit of sales account.

If desired, the bags and values may be segregated into grades and these totals may be accumulated for the cash journal entry.

By this method one operation on a typewriter produces an invoice, a ledger account and a record of sales quite as safe as
Accounting in the Peanut Industry

and preferable to a ledger, because in this case the ledger contains only clearly defined open accounts and the sales record is most complete and comprehensive.

In addition to these forms and records there are also the usual office records for notes receivable and payable, payrolls, insurance policies and analysis of expense, including of course a general ledger. Because there is nothing unusual in the accounting work except as noted I have not gone into its further detail.

Until recent years it was the practice of many factories to use the peanut hulls for fuel, and the supply was in most cases equal to the needs.

About three years ago it was ascertained that the hulls after being ground into a fine meal made a most desirable and effective absorbent, which almost immediately attracted the attention of manufacturers of tin plate.

Among the finishing processes in the manufacture of tin plate is an oil bath. Removal of the surplus oil is not only desirable but necessary. The absorbent quality of peanut hulls appealed to the tin-plate manufacturers and created such a demand for hull meal that mills for its production came into being and contracts were entered into through which the factories were enabled to change their steam-producing medium from hulls to coal.

Some of these contracts were peculiar because of the fact that the purchase price of hulls was dependent upon the cost of the substituted fuel, adjustments in the billing price at stated intervals being provided. This arrangement seems to have worked to the material benefit of the factories, because of more economical conduct of the boiler room brought about by the reduction of volume of fuel handled. In some cases it became a source of net income.

When it is understood that a comparatively small factory whose invested capital does not exceed two hundred and fifty to three hundred thousand dollars is quite likely during the short, rush, buying season to make purchases for spot cash aggregating a million dollars or more, the question of finances becomes a most serious one and adequate bank accommodation is a stern necessity. This requires either collateral in the form of storage warehouse receipts or acceptable individual endorsement, and sometimes both.
Uniform Accounting for Retail Coal and Lumber Trade*

By Robert S. Pasley

The business problems and difficulties of the retail dealers and particularly his prices are of vital interest to most of us in these days of the diminishing purchasing power of the dollar. It is true that when the retailer acquires the special commodity he handles, it already carries a heavy burden made up of all the costs and all the profits of all who have dealt in it before. He completes the magic process by adding his costs and his profit and then courageously breaks the news of the selling price to the ultimate consumer. It can be seen, then, that, if the costs and percentage of profit calculated by the retail dealer are erroneous, the consumer suffers. This is so whether the resultant price is too high or too low. If too high, the dealer is profiteering at our expense. If too low, the dealer, and possibly his creditors, make a loss which has to be made up somehow. When a loss has to be made up somehow the consumer usually pays the bill.

The average man realizes that the price of an article to him in addition to its cost of production should carry a proper percentage of profit to recompense all who have had a part in the bringing of that article to his doorstep. He becomes incensed, however, if he has reason to believe that the price of that particular article has been fixed by guesswork; for experience has taught him that in a guessing contest on the part of others he will be the loser. It is obvious, then, that anything which will serve to increase the accuracy of the retailer's knowledge of his business, upon which he bases his selling price, will help the retailer and will please the dealer's customers. I believe it is almost self-evident that accounting along uniform lines, by any branch of industry, is a step forward in the ascertainment of accurate costs—and accurate costs should be the groundwork of a reasonable selling price.

I am moved to treat particularly, in this article, of the retail

* A thesis presented at the November, 1919, examinations of the American Institute of Accountants.
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c coal and lumber industry because I have come in contact in a professional way with the educational work relative to uniform accounting that is now being accomplished by two associations of retail coal and lumber dealers within their own membership. Neither association, however, has yet succeeded in putting such a plan into effect among its members. It is encouraging, though, to note that the importance of accurate accounting is being recognized by trade associations and that each member thereof is being gradually educated to the point where he recognizes the fact that his system of accounts or lack of system bears a direct relation to his success or failure.

In comparison with other retailers the coal and lumber dealer requires a fairly large capital to conduct his business. He needs considerable space and much equipment both for receiving and storing his materials and for the delivery of them. As his dealings are generally with the householder rather than with the business man as such he may be taking considerable risk on the collection of some of his accounts. A year ago he was under regulation by the fuel commissioner as to his receipts and deliveries and may be again. He suffers as much as if not more than those engaged in other industries from strikes and uncertain labor conditions, and the labor problem is further complicated to him by the seasonable nature of his wares. With, perhaps, more than the average difficulties confronting retailers, the coal and lumber merchant cannot afford inadequate accounting.

Trade associations have done much toward broadening the minds of business men, particularly in their relations with their competitors. The business man of to-day realizes that he may learn or unlearn much from his competitor and that his competitor may learn much from him—a relation that is mutually advantageous. This is not the attitude of mind that prevailed some years ago. Then the members of the same trade or industry, if not exactly suspicious of each other, apparently felt that the imparting of knowledge to their competitors detracted from their own store of that scarce commodity. If that state of mind existed to the same extent now, the retail coal and lumber dealer would not derive as much benefit from a uniform system of accounts as he might. A comparison of unit costs (possible only where systems of uniform accounting are in effect) leads to an interchange of ideas, among the members, which is bound to prove
beneficial to many. The benefits accruing therefrom would ultimately reach the consumer.

It may be argued that the price charged for coal in any district is about the same by each dealer in that district, that about a year ago the rate to the consumer was determined by the fuel commissioner and that the individual retailer could not influence the price one way or another no matter how well he knew his costs.

Let us suppose the unregulated price of coal, as charged by all retailers in a particular district, is substantially the same. It is probable that most of the dealers are following the lead of one or two without question as to whether the rate has been determined scientifically or not. Even though the prices charged by the leaders are fair to themselves and allow a reasonable profit, the same prices charged by another retailer may be suicidal or unnecessarily high. If this particular dealer calculated on the basis of his own costs a price which was so much higher than his competitors’ that his sales suffered, he would naturally endeavor to ascertain in what respects his business was less economically administered. If the price so determined was much lower than his competitors’ he should make sure that he was not omitting from his calculations of costs items of expense such as bad debts, depreciation, etc., which, although not paid in cash, are nevertheless real expenses.

The fact that the fuel commissioner arranged prices covering certain districts is not an argument against the dealer’s knowing his costs and having accounts uniform with the other dealers—indeed, it is an argument in favor of such accounts. How did the fuel commissioner of a certain territory arrange the price of coal for that territory? He procured figures of costs from the dealers themselves and from this information determined the selling price. It was required that all the dealers submit costs per ton, made up of cost of coal at dock, handling charges, degradation, delivery expense, wages, salaries, rent, depreciation and all other expenses, but the items entering into each expense classification were left to the interpretation of the individual dealer.

Now, remember that these dealers had not a uniform accounting system. What was the result? Some dealers knew how to ascertain the cost of degradation, i. e., loss in weight or conversion of one class of coal into a smaller and cheaper grade;
Uniform Accounting for Retail Coal and Lumber Trade

others did not. Some included as part of their delivery expense the depreciation on their trucks; others included such depreciation in depreciation on plant account and some ignored it completely; no two could be said to agree on the same rate. Some were able to calculate approximately the difference in delivery cost between coal delivered by chuting and coal carried. If the dealer operated under the corporate form his salary as an officer was included as expense; the dealer operating as a single proprietor or one of a co-partnership received no salary as such, and no salary was included in the expenses submitted. Some rented their yards; others owned them. Rent was included in the one case but not in the other—and so on. One can see from this how onerous the duties of fuel commissioner must have been, and, no matter how careful was his investigation, the price as finally determined from the average of the figures submitted necessarily worked a hardship in some cases.

As a matter of fact, we know that under normal conditions the retail price of coal and lumber varies, even in the same locality. If the prices are ever to come down it will be because one dealer can afford to charge lower rates than his competitors—not because he does. It is important to the public that the dealer charging the lower rate should at the same time make a fair profit, for price-cutting that has not a sound basis is dangerous to the consumer as well as to the trade. I believe that, following the general adoption by coal and lumber retailers of a plan of uniform accounting, intelligent competition would be one of the important results. All competition is not intelligent. I have said before that the ultimate consumer pays all the bills—unintelligent competition leaves many unpaid bills in its wake. By intelligent competition I mean reductions in rates brought about by economical administration.

Uniform accounting does not mean that each dealer should keep exactly the same accounts as his competitor, with no latitude to cover the needs peculiar to each one. It does mean, however, a thorough understanding of the items to be included under each expense classification, so that, from the accounts of each, operating costs may be prepared under classifications of expense that do not mean one thing for one dealer and something different for another. Briefly, the accounts of each should speak the same language.

To ensure to the dealer and his public all the benefits result-
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ing from a system of uniform accounting, the trade association should require every member to compile, periodically, operating costs per ton spread over stated expense classifications. These unit prices should be compared and discussed at the meetings of the association.

For instance, when the delivery unit per ton for one dealer is read all the others know that every kind of expense they have included under that classification is embodied therein. Any real variation existing then between the dealers on this unit immediately raises an interesting and educational discussion as to the reason therefor. One dealer may have a large number of customers for whom coal can be chuted—his delivery rate per ton should be less than the one who has to carry most of his deliveries. It might be possible to use this information to determine for a special district a fair charge for carrying. Some interesting comparisons might be made, also, of the cost of delivery by motor or by horse-drawn trucks.

A comparison of unit costs under a uniform accounting plan, as read at an association meeting, removing from the minds of the retailers, as it would, any uncertainty as to what might be contained in the corresponding expense classifications of their competitors, presents an opportunity for really constructive work.

Still confining ourselves to the classification "delivery expense," it may be found that a wide variation exists in this unit between two dealers in the same district with approximately the same tonnage handled and other circumstances almost equal. The retailer with the higher cost can investigate his delivery expense until he discovers the particular item or items that are responsible. Having found the items that are high he can then investigate the cause. He may find that his competitor has the knack of handling his employees so that he receives from them the maximum of service; or that his competitor has a lower motor maintenance cost because he takes some practical precautions in the care of his trucks; or that his competitor plans his routing scientifically, whereas his own methods are haphazard. If, as a result of this investigation, the retailer with the higher delivery cost takes to himself the lessons he has learned and improves his delivery methods, who will say that he is the only one to derive benefit therefrom? Let us not forget who it is that pays for the mistakes of the retailer in every line of industry.
Depreciation Reserves and Rising Prices

By Ernest S. Rastall

In regard to reserves for depreciation of plant it has been argued that in times of rising prices operating expense should be charged with the expected cost of renewals, regardless of the original cost of the property, in order to maintain the plant in its physical condition and capacity as a producing agent.

It is pointed out that at such times income feels the stimulating effect of rising prices before costs do, and that therefore the increase of profits is apparent rather than real because costs must ultimately be met.

The contention is that generally speaking the purpose of reserving from profits an amount sufficient to cover depreciation is to maintain the physical plant and keep up production without drawing upon capital funds.

This argument insists that the increase in cost of replacement over original cost should not be added to capital account; that the only way to withhold from earnings sufficient to cover renewal costs is to charge operating account, and, failing in this, the only recourse is to draw upon capital funds through the issuance of new securities, presumably bonds, and that interest on these bonds will be an added expense burden upon future operations; that to do otherwise in times of rising prices constitutes a waste of capital and consequent loss of earning power and that if in the future a dollar will possess only half its present purchasing power the future stockholders should be provided with two dollars in the place of one.

For the stockholders to exercise a restraint upon extravagance and reserve a portion of their profits so newly and so easily acquired against a day of reckoning is commendable, but why should they do this under the guise of a reserve for depreciation of something that is already written off the books and from the standpoint of pure bookkeeping no longer exists? To set up a replacement reserve or even an enlargement reserve by a debit to surplus and a credit to reserve would be permissible, but it
would not be correct procedure to charge it to surplus via the operating route.

When prices are seen to be rising, prudent stockholders will, of course, reserve from earnings enough for replacement needs, but this should not all be charged to operation.

To charge operating with the expected cost of renewals, if that were greater than the original cost of the property consumed in service, would have the effect (a) of creating a reserve for depreciation larger than the property depreciated, (b) of affording the company a pretext for passing along to the consumer the cost of increasing the capital investment of the company in the form of a secret reserve, (c) of tempting future stockholders to reverse the whole procedure by reappraisal of the property by a debit to plant and a credit to surplus.

If a property which cost $5,000 and is estimated to last twenty years, is written off at the rate of 10 per cent per annum for twenty years, because it is expected that it will cost $10,000 to replace it at that time, the bookkeeping effect would be to show at the end of twenty years an asset of $5,000, and a reserve for depreciation of that identical asset of $10,000. Supposing the property to have actually worn out and disappeared, its place in the balance-sheet would have been filled by some other asset, probably of a very liquid nature, which the company could convert into another piece of property of double money worth if it wished. When purchased this would be charged to reserve account and cancel it, and the balance-sheet would still show an asset of $5,000, which actually cost $10,000.

There is a distinct difference between reserves for depreciation and reserves for renewals. The latter is a broader term; and while it does connote the same idea as the former up to a point where it equals the original cost, it connotes a very different idea after that point is passed.

If reserve is credited with $10,000 and replacement charged against it, the plant value stands on the balance-sheet unchanged at $5,000.

On the other hand, if reserve for depreciation is only $5,000, and if it is charged with $5,000 and plant is also charged with $5,000 at the time of replacement, the balance-sheet showing is then $10,000. An earning of 6 per cent on the former would be
Depreciation Reserves and Rising Prices

but 3 per cent on the latter. It is apparent therefore that the latter position holds the stronger justification for a request for increase of rates charged to the public.

In the former case the future stockholder would be in a position to ask for a return upon an investment of $5,000, and in the latter $10,000. The status of the future stockholder in the former case is that he has fallen heir to a property worth $10,000 stated on the books at $5,000, and he would be sure to request a reappraisal on actual replacement cost values with a corresponding credit to surplus and to request an adequate return upon the full amount. This would then operate actually to reverse the entry which charged operating and credited reserve for depreciation.

If the replacement cost of such a property advanced at the rate of 5 per cent a year there would be no harm in debiting plant and crediting reserve with that amount, provided this addition to capital were not included when writing off subsequent depreciation.

A company that finds that through its reserves it has saved only enough liquid assets with which to repurchase the equivalent in money of its worn-out plant, but that to replace the equivalent physical property will require double that amount, faces the need of finding more capital either in the other savings expressed in surplus account or in the issuance of additional securities, either stock or bonds.

It must be borne in mind, however, that borrowed capital is the same as invested capital. Interest on bonds, if capital is secured that way, is not an expense burden upon operation, but a division of profits with those who furnish it.

While there remains $5,000 of the original invested capital, even though that be mere money value and not plant value, it is an error to say that the stockholders have been living on capital instead of income.

To charge operating with that part of an expected replacement cost which exceeds actual cost would be to understate actual profits and would in all probability, in the case of a public utility, give great license to those who are permitted to estimate the expected increase not only to pass on to the consumer the cost of increasing the actual invested capital but allow a return, the
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purchasing power of which would be the same as in the days of lower prices. To permit this would be to put the stockholders of a company, which is thus able to pass along the burden to the consumer, in a position of great advantage over those whose investments did not permit of such a change, as, for instance, the widow who owns a 6 per cent mortgage or the owner of government bonds. To deduct the amount from income instead of from profit, would also give the possessor of such shares an unfair advantage in regard to income tax, for how could the widow maintain the purchasing power of her income and avoid a tax in any similar manner?

In other words, if the dollar has fallen in value, such people would have the advantage over those who are not able arbitrarily to increase the number of dollars of their investment and thus maintain an even purchasing power.

The iniquity of rising prices lies in the unevenness with which they rise. Those who are in a position to be the first to raise their prices thereby secure an advantage over others through the increase of purchasing power which it gives them. If all people were simultaneously to raise the prices of what they sell an equal percentage, no harm would result. The demand for war materials gave to certain manufacturers the opportunity not only to sell at higher prices but to sell materials which in ordinary times would be junk.

The demand for men in the army gave to the vendors of labor the next chance. Manufacturers were compelled to bid high for labor but saved themselves by passing the burden along (with a little added for their own comfort) to the consumer. When the laborer who thus received larger wages was the consumer no harm was done—the thing simply operated to tax him to pay himself. Those who were not in a position arbitrarily to increase their prices were the ones who paid the bill. The stockholders of companies which manufactured war supplies had the advantage over all others. The artisans in such factories had the advantage over other artisans who worked for the makers of "non-essentials." The artisan had the advantage over the office clerk, the school teacher and the widow with a small income and others not in a position arbitrarily to multiply the dollars of their invested capital.
EDITORIAL

Advertising

No question is more generally the topic of discussion among accountants than the propriety or impropriety of advertising. During the past year there seems to have been a recrudescence of the advertising idea among certain members of the profession, and this magazine has received many inquiries from persons who deplore the prevalence of advertisement, but seem to dread the effects of it upon their own individual practice.

In the American Institute of Accountants matters of this kind are under the supervision of the committee on professional ethics, and in view of the wide-spread interest which is manifested in the question of advertising, the chairman of that committee was asked to express his opinions for publication.

We are glad to be able to publish the views of the chairman of the committee on professional ethics, and in doing so commend them to the earnest consideration of all accountants who are not sure that advertising is undesirable.

The opinion follows:

The question of the proper kind of publicity for a professional accountant has before now been discussed by this Journal. It is a question which is much in the mind of every accountant and cannot be too frequently discussed.

That the great preponderance of opinion among reputable accountants, leaders in their profession, is opposed to commercial advertising of all kinds is beyond question. That some able and competent practitioners—yes, even members of the institute—as well as many professional quacks and immature and ill-informed
members of the profession, deem it essential to advertise their wares in some form or another is unfortunately also true.

The specious arguments which are made in favor of advertising and publicity campaigns are sometimes presented in such alluring form as to silence, if not convince, those who know in their hearts that no calling or vocation can consistently aspire to a professional status and dignity while it countenances unprofessional and undignified practices. Oil and water will not mix—you cannot wed science to charlatanry without producing a sterile hybrid, and you cannot lay claim to membership in a profession while engaging in unprofessional practices. The things are incompatible—they cannot be reconciled, no matter how ingenious and eloquent the argument.

The following letter was recently received from a member of the institute:

Sir:—I am moved to write this letter because of the action of many accountants, some C P A’s and members of the institute and others who are not.

There has been much recent discussion, oral and written, as to ethics in our profession, embracing among other things the question of advertising, circularizing and other forms of publicity.

In my twenty-five years of practice I know I have been as conservative as any member of the profession, and have watched the various forms of publicity and advertising by fellow accountants and witnessed the receipt by my own clients of all manner of circulars and pamphlets soliciting business, and have consistently stood firm in my attitude.

I am, however, at present, going through a period of deep thinking caused by methods and practices of other accountants, and am wondering whether I have been and am still too conservative in my ideas and methods, and whether I should adopt different methods by advertising, circularizing, etc., with a view to increasing my business—not that I am in need of more business, but merely for the purpose of having a larger business with a larger number of assistants and a larger suite of offices, all of which, of course, would mean more income.

My present state of mind is also caused by the fact that my son, now in practice with me after having been graduated from college and been in the service for more than two years, is very observing, ambitious and likes the profession, and tells me frequently I am, in his judgment, too conservative, when he observes the publicity of other accountants. We all must admit that many of them do secure considerable new business, and he is fired with the ambition to enlarge the field and build up a larger practice than we now have.

By this letter you will recognize that I am still conservative, by seeking the opinion of those whose opinions are worth while, instead of being carried away with the new ideas and undertaking a campaign of publicity.

I should appreciate a letter from you on the subject, or if you think it better to have it referred to the proper committee you may do so, and if it would make good material for an article for discussion in The Journal of Accountancy it might be of some service not only to myself but to many other members of the profession, because it must be a fact that many others
Editorial

are doing some hard thinking along the same lines, and it seems to me this is as good a time as any other to have the matter discussed and handled in the dignified and commendable manner in which every subject is handled by the institute.

Also witness the numerous men leaving the service of the internal revenue bureau and advertising by letter and other means that they are now available to the business world, setting forth in glowing terms the wonderful and valuable work they are qualified to do.

The foregoing letter was followed by another several weeks later containing a dozen or more samples of newspaper clippings ranging from a one-inch card to a full-page display advertisement:

It reads:

Just a few samples of the kind of advertisements, which are the cause of my recent letter to you.

Professional ethics—does not seem to be any such animal—and my long continued conservatism and dignified observance of ethics in the profession are weakening and waver more every day.

The foregoing correspondence parallels the line of argument so frequently made by those practitioners whose innate good taste and professional instincts would naturally lead them to refrain from such lurid methods, but who say to themselves: “The advertiser is depriving me of opportunities for my services and I must, in self-defence, climb the hill of printers’ ink and shout my wares.” How often have we heard this argument. And how seductive it is.

The discriminating public long ago learned properly to classify the advertising doctor, dentist, architect, engineer or lawyer—and yet there are alleged members of each profession who contribute to filling the advertising pages of our daily newspapers. Who among the readers of this editorial is ever allured into patronizing an advertising dentist? If there be one, we think he lost his way when he became a reader of this JOURNAL. It is not the type of man who reads this magazine to whom such publicity appeal is made. It may be that the business public has not yet quite reached the stage of discrimination it is in concerning the question of advertising practitioners of the older professions. The time is bound to come when it will be. Do you want to be among the leaders or among the laggards?

While it is true that many accountants, including members of the institute, do more or less advertising, the best opinion does not look with favor upon this practice. You are not likely to patronize an advertising doctor or lawyer, and the same reasons which would dissuade any member of these older professions
from commercializing his profession by promiscuous advertising should dissuade a member of our profession from resorting to such undignified procedure.

Consider for a moment what the result would be if every practitioner were to advertise to the same extent. What possible profit could ever flow to anyone except as the result of more skillful and conscientious work? The artistic and skillful advertiser may reap a momentary financial advantage at the expense of practitioners who do not advertise. We are sure that if he does it is quite likely to be at the expense of his professional reputation, and we take it that every accountant has quite as much regard for his professional reputation as for his financial success.

The accountant who advertises obtains business by this means solely because his advertisement does not come into competition with advertisements of his more dignified fellows. If all advertised, his advertisement would not attract the attention which it now does attract. If we admit this to be so, we place the advertising accountant in the position of taking advantage of his fellows.

This kind of thing may be good commercial practice, but does it add anything to the dignity and the fellowship of a profession? From this point of view, does not the advertising and soliciting accountant come pretty close to being a bandit or, in the vernacular of another profession, the "ambulance chaser" of the accounting profession?

However, the outstanding point about this whole matter is that either accountancy is a profession or it is not a profession. Its practitioners will, therefore, have to choose which it shall be. If it is to be a profession, it must adopt professional practices. If it is to be a trade, advertise and shout your wares from the house tops, but do not delude yourself into the belief that you are a member of a dignified and learned profession.

"Time at last sets all things even," and the writer has an abiding faith that in the long run the accountant who steers his own northwest course and keeps to the charted channels will have quite as successful a voyage as though he departed from the approved and tested routes and sought a short-cut to professional success.
Income-Tax Department

Edited by John B. Niven

New forms for 1919 income-tax returns will without doubt be in the hands of collectors before this number reaches its readers. There is no new consolidated issue of the regulations, but all the amendments and revisions of regulations 45 which have been promulgated up to December 2, 1919, since the bound copies of that volume were issued April 17, 1919—all of these amendments have been published in these pages—have been issued in pamphlet form as Addenda to Regulations 45, and should be procurable from local collectors.

Liberty Bond Exemptions

The subject of taxable interest on Liberty bonds offers some complications. A table describing the various issues and showing the different exemptions in graphic form has been drawn up and is presented herewith. It shows those exemptions which are "specific," applicable to a single issue only, and those which are "group" exemptions or "joint and several." "Group" exemptions are either "conditional" or "unconditional." Unconditional group exemptions and specific exemptions are valid whether the bonds on which the interest is received or any other holdings of bonds are still retained or have been sold. Conditional exemptions depend upon the retention, at the time the taxpayer's return is rendered, of originally subscribed fourth or Victory loan bonds.

Taxable interest should be calculated on the accrual basis, even though credited on the books of the taxpayer only as collected. If the instructions for the calculation contained in the income-tax blanks are followed literally, the throwing of the difference between the taxable interest and the book interest into the income reconciliation—it may be an addition to book income as well as a deduction therefrom—automatically adjusts the taxable income to the accrual basis, regardless of the method used in the books.

Treasury Decisions

It may not be generally realized that income-tax returns are "public records and . . . open to inspection as such." This is in section 257 of the revenue act of 1918; but the accessibility is more apparent than real, being possible "only upon the order of the president, under rules and regulations to be prescribed by the secretary of the treasury and approved by the president."

The new treasury decisions are largely taken up with the regulations formulated under this proviso, prescribing, first, who may have access to income-tax returns for the purpose of inspection, and under what conditions, and, second, to whom copies of returns may be furnished. (T. D.'s 2961-2.)

The maker of a return is always entitled to a copy of his return, but
The maximum exemptions indicated are from "additional" taxes; that is, individual surtaxes and corporation excess-profits and war-profits taxes. All issues are exempt from (normal) income tax. 3 3/4% bonds (first issue) are also exempt. 3 3/8% notes (Victory loan) from all "additional" taxes.

<table>
<thead>
<tr>
<th>Issue</th>
<th>Description of issue</th>
<th>Date of issue or conversion</th>
</tr>
</thead>
<tbody>
<tr>
<td>First 3 3/4's................</td>
<td>Original issue</td>
<td>June 15, 1917</td>
</tr>
<tr>
<td>First converted 4's.........</td>
<td>First 3 3/4's converted into second 4's.</td>
<td>Nov. 15, 1917</td>
</tr>
<tr>
<td>First converted 4 1/2's.....</td>
<td>First 3 3/4's converted into third 4 1/2's issue of May 9, 1918.</td>
<td>May 9, 1918</td>
</tr>
<tr>
<td>Second 4's..................</td>
<td>Original issue</td>
<td>Nov. 15, 1917</td>
</tr>
<tr>
<td>Second converted 4 1/2's....</td>
<td>Second 4's converted into third 4 1/2's issue of May 9, 1918.</td>
<td>May 9, 1918</td>
</tr>
<tr>
<td>Third 4 1/2's................</td>
<td>Original issue</td>
<td>May 9, 1918</td>
</tr>
<tr>
<td>Fourth 4 1/2's.............</td>
<td>Original issue</td>
<td>Oct. 24, 1918</td>
</tr>
<tr>
<td>First Liberty second converted 4 1/2's.</td>
<td>First 3 3/4's converted into fourth 4 1/2's issue of Oct. 24, 1918.</td>
<td>Oct. 24, 1918</td>
</tr>
<tr>
<td>Treasury certificates .....</td>
<td>Original issue</td>
<td></td>
</tr>
<tr>
<td>War savings certificates</td>
<td>Original issue</td>
<td></td>
</tr>
</tbody>
</table>

**DURATION OF EXEMPTIONS**

<table>
<thead>
<tr>
<th>Exemptions begin</th>
<th>Exemptions terminate</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) With date of respective issues</td>
<td>(d) 2 years after end of war</td>
</tr>
<tr>
<td>(b) January 1, 1918</td>
<td>(e) 5 years after end of war</td>
</tr>
<tr>
<td>(c) January 1, 1919</td>
<td>(f) At termination of life of Victory loan notes on which based.</td>
</tr>
<tr>
<td></td>
<td>(g) Unlimited (during life or holding of respective issues).</td>
</tr>
</tbody>
</table>

the right of inspection granted others also includes the right to copy or to extract data from the return. Besides the maker and the necessary officers and employees of the treasury department, the right of inspection extends
**Income-Tax Department**

**MAXIMUM TAX EXEMPTIONS THEREON**

4\% ¾ notes (Victory loan) are entitled to no exemption from "additional" taxes.

4 \% and 4\% ¾ bonds are exempt from "additional" taxes to the extent indicated in the table.

Specific exemptions: Applicable to a single issue only.

Group exemptions: Applicable to all or any issue of the group indicated.

<table>
<thead>
<tr>
<th>Interest due</th>
<th>Maturity</th>
<th>SPECIFIC</th>
<th>GROUP</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Unconditional</td>
<td>Conditional</td>
</tr>
<tr>
<td>Jun. 15</td>
<td>June 15</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 15</td>
<td>December 15, 1932-1947</td>
<td></td>
<td></td>
</tr>
<tr>
<td>June 15</td>
<td>June 15</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 15</td>
<td>December 15, 1932-1947</td>
<td></td>
<td></td>
</tr>
<tr>
<td>June 15</td>
<td>June 15</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 15</td>
<td>December 15, 1932-1947</td>
<td></td>
<td></td>
</tr>
<tr>
<td>May 15</td>
<td>Nov. 15</td>
<td>$30,000. (a)</td>
<td></td>
</tr>
<tr>
<td>Nov. 15</td>
<td>November 15, 1927-1942</td>
<td></td>
<td></td>
</tr>
<tr>
<td>May 15</td>
<td>Nov. 15</td>
<td>$45,000. (b)</td>
<td></td>
</tr>
<tr>
<td>Nov. 15</td>
<td>November 15, 1927-1942</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mar. 15</td>
<td>Sept. 15</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sept. 15</td>
<td>September 15, 1928</td>
<td></td>
<td></td>
</tr>
<tr>
<td>April 15</td>
<td>Oct. 15</td>
<td>$30,000. (d)</td>
<td></td>
</tr>
<tr>
<td>Oct. 15</td>
<td>October 15, 1928-1928</td>
<td></td>
<td></td>
</tr>
<tr>
<td>June 15</td>
<td>June 15</td>
<td>$30,000. (a)</td>
<td></td>
</tr>
<tr>
<td>Dec. 15</td>
<td>December 15, 1922-1947</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Group exemptions:

- All
- Conditional on original subscription and continued holding at date of (making) tax return of:
- Two-thirds as many bonds of the Fourth Liberty loan.
- One-third as many bonds of the Victory Liberty loan.

Recapitulation: Total Possible Exemptions

<table>
<thead>
<tr>
<th>Prior to Jan. 1, 1919</th>
<th>Additional beginning Jan. 1, 1919</th>
<th>Total from Jan. 1, 1919</th>
</tr>
</thead>
<tbody>
<tr>
<td>Specific</td>
<td>$ 60,000.</td>
<td>$ 60,000.</td>
</tr>
<tr>
<td>Unconditional</td>
<td>$ 200,000.</td>
<td>$ 30,000.</td>
</tr>
<tr>
<td>Conditional</td>
<td>$ 45,000.</td>
<td>$ 20,000.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$ 65,000.</td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>$110,000.</strong></td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>$50,000.</strong></td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>$160,000.</strong></td>
</tr>
</tbody>
</table>

To a duly constituted attorney in fact, an administrator, executor, trustee or his attorney, and under certain conditions to an heir at law or next of kin. A stockholder holding as little as one per cent of a corporation's stock
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may, under section 257 of the law, examine the return of his corporation; but he must satisfy the department as to the bona-fides of his request and must apply in person only, not by proxy.

Whether departments of the government other than the treasury may be granted the privilege of inspection depends on the conditions in each case; but the United States is free to use the returns in litigation, this right being implicit in their status of "public records." The privilege of states "imposing an income tax" of having access to the returns is also contained in the law, section 257.

A taxpayer who received all in one year a sum of money not previously agreed on as compensation for services over a period of years has been obliged to report the entire amount as income for the year in which it was received, and the assessment has been confirmed by a decision of the United States district court. The case depended on the fact that the taxpayer kept no books of account, under which conditions the revenue act of 1918 states the computation of income shall be made in such a manner "as in the opinion of the commissioner does clearly reflect the income," and the commissioner's relevant "opinion" is set forth in article 32 of regulations 45: "where no determination of compensation is had until the completion of the service the amount received is income for the calendar year of its determination." (See T. D. 2960.)

Where, in cases of corporate "reorganization," new stock of no greater par value than the old stock is received in exchange for it, there is (section 202b) no gain or loss at the time; but the gain or loss is determined on subsequent sale of the stock, as explained in article 1568. This article has been amplified in T. D. 2963 to provide for allocation of the cost (or March 1, 1913, value) of the original securities to the different classes of new securities, if more than one class is issued; the allocation being made in proportion to the relative market values of each class of securities as compared with the total market value.

TREASURY RULINGS
(T. D. 2960, January 7, 1920)

Income Tax—Decision of Court

Jackson v. Smietanka (U. S. district court, December, 1919)

When Income Taxable.

A taxpayer who keeps no books of account, and to whom is paid, upon the termination of services extending over a period of years, a lump sum in amount not previously agreed upon, as compensation for such services, must return as income in the year in which received, the entire amount so paid him, even when such payment is accompanied by a statement proportioning the compensation over the years in which the services were rendered.

The appended decision of the United States district court for the eastern
division of the northern district of Illinois, in the case of *Jackson v. Smietanka*, is published not as a ruling of the treasury department, but for the information of internal-revenue officers and others concerned.

**United States District Court, Eastern Division of Northern District of Illinois. No. 33109**

*William J. Jackson v. Julius F. Smietanka, collector of the United States internal revenue, first district of Illinois*

Page, circuit judge: This is a demurrer to the declaration.

The sole question involved in this case is, Was plaintiff erroneously taxed under the revenue law of 1918, or should he have been taxed under the several laws of the years 1913 to 1918, as plaintiff contends, on an income received as follows:

Plaintiff was on May 27, 1913, appointed a receiver of the C. & E. I. R. R. Co. and served until April 27, 1918, for which he received under the order of the district court, dated August 4, 1913, $2,000 per month, commencing July, 1913, to be received on account, with the liberty on his discharge to apply for further compensation. When he resigned a general order was entered, on April 27, 1918, allowing him an additional compensation of $100,000. That general order was amended by order of April 22, 1919, as follows:

That said services of said William J. Jackson as receiver were rendered continuously from May 27, 1913, to and including April 27, 1918, and the compensation therefor now allowed was earned and accrued as follows: In the year 1913, $12,144.85; in the year 1914, $20,334.26; in the year 1915, $20,334.26; in the year 1916, $20,334.26; in the year 1917, $20,334.26; in the year 1918, $6,518.11.

That amendment was entered as of April 27, 1918. The petition for the amended order was filed and the order made long after the tax was assessed. The government was not a party thereto.

Plaintiff cites section 206 of the revenue law of 1918 as a basis for his contention and says, "If that section cannot reasonably be applied to such a case as that of plaintiff, we ask to what sort of a case it does apply?" Article 1641 of treasury department regulations 45, under the revenue act of 1918, says that section 206 refers to other and wholly different matters, and this interpretation is supported, and in the opinion of the court conclusively, by sections 201 and 205 of the same act, in the former of which direct reference is made to said section 206.

After specifying in detail what the gross income includes, section 213 provides:

The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period.

Subdivision (b) of section 212 provides:

The net income shall be computed upon the basis of taxpayer's annual accounting period * * * in accordance with the method of accounting regularly employed in keeping the books of such taxpayer.

Plaintiff kept no books, so that clause does not apply. It further provides that—

If no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made upon such basis and in such manner as in the opinion of the commissioner does clearly reflect the income.

The only language which might apply to plaintiff is—
The Journal of Accountancy

If no such method of accounting has been so employed * * * computation shall be made upon such basis and in such manner as in the opinion of the commissioner does clearly reflect the income.

This seems to leave the burden upon the plaintiff here to show that the method of accounting insisted upon by him has been prescribed as a basis by the commissioner.

Article 52 of regulations 45 provides:
Gains, profits and income are to be included in the gross income for the taxable year in which they are received by the taxpayer, unless they are included when they accrue to him in accordance with the approved method of accounting followed by him.

Article 32 of said regulations 45 states:
Where no determination of compensation is had until the completion of the services, the amount received is income for the calendar year of its determination.

The demurrer is sustained.

(T. D. 2961, January 7, 1920)

Inspection of Returns

Regulations governing the inspection of returns of individuals, partnerships, corporations, associations, joint-stock companies, and insurance companies made pursuant to the requirements of section 2 of the tariff act of October 3, 1913; title I of the revenue act of 1916; title II of the revenue act of 1917; and titles II and III and section 1000, title X, of the revenue act of 1918. Former regulations bearing on the same subject superseded.

Section 2 of the tariff act of October 3, 1913, imposes an income tax on individuals, corporations, joint-stock companies or associations, and insurance companies, and section 14 (b) of said title provides:
When the assessment shall be made, as provided in this section, the returns, together with any corrections thereof which may have been made by the commissioner, shall be filed in the office of the commissioner of internal revenue, and shall constitute public records and be open to inspection as such: provided, that any and all such returns shall be open to inspection only upon the order of the president, under rules and regulations to be prescribed by the secretary of the treasury and approved by the president: * * *

Title I of the revenue act of 1916 imposes an income tax on individuals, corporations, joint-stock companies or associations, and insurance companies, and section 14 (b) of said title provides:
When the assessment shall be made, as provided in this title, the returns, together with any corrections thereof which may have been made by the commissioner, shall be filed in the office of the commissioner of internal revenue, and shall constitute public records and be open to inspection as such: provided, that any and all such returns shall be open to inspection only upon order of the president, under rules and regulations to be prescribed by the secretary of the treasury and approved by the president: * * *

Title II of the revenue act of 1917 imposes a war excess profits tax on individuals, partnerships, corporations, joint-stock companies or associations, and insurance companies, and section 212 of said title provides:
That all administrative, special, and general provisions of law, including the laws in relation to the assessment, remission, collection, and refund of internal-revenue taxes not heretofore specifically repealed, and not inconsistent with the provisions of this title, are hereby extended and made applicable to all the provisions of this title and to the tax herein imposed, and all provisions of title I of such act of September eighth, nineteen hun-
expressly herewith, division excise otherwise of act ance purposes are of to of the internal returns manner, imposed companies, profits secretary order shall be made applicable to the returns and payment of the tax therein imposed, including penalties, are hereby made applicable to the tax imposed by this title.

Title II of the revenue act of 1918 imposes an income tax on individuals, associations, joint-stock companies, and insurance companies, and section 257 of said title provides:

That returns upon which the tax has been determined by the commissioner shall constitute public records; but they shall be open to inspection only upon order of the president and under rules and regulations prescribed by the secretary and approved by the president. * * *

Title III of the revenue act of 1918 imposes a war profits and excess-profits tax on corporations, associations, joint-stock companies, and insurance companies, in addition to other taxes imposed by the act, and section 336 of said title provides:

That every corporation, not exempt under section 304, shall make a return for the purposes of this title. Such returns shall be made, and the taxes imposed by this title shall be paid, at the same times and places, in the same manner, and subject to the same conditions, as is provided in the case of returns and payment of income tax by corporations for the purposes of title II, and all the provisions of that title not inapplicable, including penalties, are hereby made applicable to the taxes imposed by this title.

Section 1000, title X, of the revenue act of 1918 imposes on corporations a special excise tax with respect to carrying on or doing business, and subdivision (d) of said section provides:

Section 257 shall apply to all returns filed with the commissioner for purposes of the tax imposed by this section.

Pursuant to these provisions of law the president orders that returns of individuals, partnerships, associations, joint-stock companies, and insurance companies filed under the provisions of section 2 of the tariff act of October 3, 1913; title I of the revenue act of 1916; title II of the revenue act of 1917; and titles II and III and section 1000 of title X, of the revenue act of 1918, or under laws hereafter enacted in substitution or amendment of the income tax or capital stock tax provisions thereof and not inconsistent herewith, shall be open to inspection in accordance and upon compliance with the following rules and regulations:

1. These regulations deal only with inspection of returns, as the statutes expressly require the approval of the president of regulations on this subject. Other uses to which returns may be lawfully put, without action by the president, are not covered by these regulations.

2. The word "corporation" when used alone herein shall, unless otherwise indicated, include corporations, associations, joint-stock companies, and insurance companies. The word "return" when so used shall, unless otherwise indicated, include income and profits tax returns; and also special excise tax returns of corporations filed pursuant to section 1000, title X, of the revenue act of 1918.

3. Written statements filed with the commissioner of internal revenue designed to be supplemental to and to become a part of tax returns shall be subject to the same rules and regulations as to inspection as are the tax returns themselves.

4. Except as hereinafter specifically provided, the commissioner of internal revenue may, in his discretion, upon written application setting forth fully the reasons for the request, grant permission for the inspection of returns in accordance with these regulations. The application will be considered by the commissioner and a decision reached by him whether the applicant has met the conditions imposed by these regulations and whether the reasons advanced for permission to inspect are sufficient to permit the inspection. Such written application is not required of the officers and
employees of the treasury department whose official duties require inspection of a return, or of the solicitor of internal revenue.

5. The return of an individual shall be open to inspection as follows:

(a) By the officers and employees of the treasury department whose official duties require such inspection and by the solicitor of internal revenue; (b) by the person who made the return, or by his duly constituted attorney in fact; (c) by the administrator, executor, or trustee of the taxpayer's estate, or by the duly constituted attorney in fact of such administrator, executor, or trustee, where the maker of the return has died; and (d) in the discretion of the commissioner of internal revenue, by one of the heirs at law or next of kin of such deceased person upon showing that he has a material interest which will be affected by information contained in the return.

6. A joint return of a husband and wife shall be open to inspection (a) by the officers and employees of the treasury department whose official duties require such inspection, and by the solicitor of internal revenue; and (b) by either spouse for whom the return was made, or his or her duly constituted attorney, upon satisfactory evidence of such relationship being furnished.

7. The return of a partnership shall be open to inspection (a) by the officers and employees of the treasury department whose official duties require such inspection and by the solicitor of internal revenue; and (b) by any individual (or his duly constituted attorney in fact or legal representative) who was a member of such partnership during any part of the time covered by the return, upon satisfactory evidence of such fact being furnished.

8. The return of a corporation shall be open to inspection (a) by the officers and employees of the treasury department whose official duties require such inspection and by the solicitor of internal revenue; (b) upon satisfactory evidence of identity and official position, by the president, vice-president, secretary or treasurer of such corporation, or, if none, its principal officer; and (c) by a stockholder of such corporation as provided in paragraph 9 hereof.

9. A stockholder of record owning 1 per cent or more of the stock of the outstanding stock of a corporation may be permitted to inspect its return. Such permission will only be granted upon an application in writing to the commissioner of internal revenue accompanied by an affidavit showing applicant's address, the name of the corporation, the period of time covered by the return he desires to inspect, and a certificate from the officials of the corporation, or other satisfactory evidence showing the amount of the corporation's outstanding capital stock, the number of shares owned by the applicant, the date when such stock was acquired, and satisfactory proof of identity. This privilege of inspection is personal and will be granted only to the stockholder. This rule has no application to the return of a corporation filed pursuant to the revenue act of 1918, specific provision, independent of presidential regulation, being made in that act for inspection by a stockholder of a return of a corporation filed thereunder (second proviso of sec. 257).

10. When the head of an executive department (other than the treasury department) or of any other United States government establishment, desires to inspect or to have some other officer or employee of his branch of the service inspect a return in connection with some matter officially before him, the inspection may, in the discretion of the secretary of the treasury, be permitted upon written application to him by the head of such executive department or other government establishment. The application must be signed by such head and must show in detail why the inspection is desired, the name and address of the taxpayer who made the return, and the name and official designation of the one it is desired shall inspect the return.
Income-Tax Department

When the head of a bureau or office in the treasury department, not a part of the internal revenue bureau, desires to inspect a return in connection with some matter officially before him other than an income, profits tax or corporation excise tax matter, the inspection may, in the discretion of the secretary, be permitted upon written application to him by the head of such bureau or office, showing in detail why the inspection is desired. The reasons submitted for permission to inspect as provided in this paragraph shall be considered by the secretary and a decision reached by him whether the reasons are sufficient to permit the inspection.

11. When it becomes necessary for the department to furnish returns or copies thereof for use in legal proceedings, inspection of such returns or copies that necessarily results from such use is permitted.

12. Except as provided in paragraph 11, returns may be inspected only in the office of the commissioner of internal revenue, Washington, District of Columbia.

13. A person who, under these regulations, is permitted to inspect a return may make and take copy thereof or a memorandum of data contained therein.

14. By section 3167, Revised Statutes, as amended by the revenue act of 1918, it is made a misdemeanor for any person to print or publish in any manner whatever not provided by law any income return, or any part thereof, or source of income, profits, losses, or expenditures appearing in any income return, which misdemeanor is punishable by a fine not exceeding $1,000 or by imprisonment not exceeding one year, or both, at the discretion of the court; and if the offender be an officer or employee of the United States, by dismissal from office or discharge from employment.

15. All former regulations bearing on the subject of inspection of returns are hereby superseded.

16. These regulations shall remain in force until expressly withdrawn or overruled.

(T. D. 2962, January 7, 1920)

Regulations governing the furnishing of copies of income returns; the giving to state officials access to income returns of corporations, associations, joint-stock companies, and insurance companies; the examination by a stockholder of the annual income returns of a corporation made pursuant to titles II and III and section 1000, title X, of the revenue act of 1918.

I. Furnishing of Copies of Income Returns

No specific provision is made in the statutes for furnishing a copy of an income return to anyone. Authority to permit inspection does not carry with it authority to furnish a copy. Implied authority to furnish a copy is contained in several provisions of law constituting returns public records, and in sections 161 and 251, Revised Statutes, which confer upon the secretary of the treasury broad power to make rules and regulations concerning "custody, use, and preservation of the records, papers, and property" of the department and the enforcement of the internal-revenue laws. Because of the provisions contained in section 3167, Revised Statutes, as amended by the revenue act of 1918, making it unlawful for any officer or employee of the United States "to divulge or to make known in any manner whatever not provided by law to any person * * * the amount or source of income, profits, losses, expenditures, or any particular thereof, set forth or disclosed in any income return, or to permit any income return or copy thereof or any book containing any abstract or particulars thereof to be seen or examined by any person except as provided by law"; and also unlawful "for any person to print or publish in any manner whatever not provided by law any income return, or any part thereof, or source of income,
profits, losses, or expenditures appearing in any income return"; a copy of an income return cannot be furnished, except as provided by law, to anyone except the person or persons who made the return. Furnishing the maker with a copy of his return is not a divulging of information contained therein to any person, within the meaning of section 3167, Revised Statutes, as amended. There are numerous provisions in the statutes constituting the doing or failure to do certain things offensive against the United States, and providing for collecting unpaid taxes by suits in court and for bringing suits to recover taxes and penalties wrongfully collected. These provisions would be of no avail were it held that the returns themselves, or certified copies thereof provided for in section 882, Revised Statutes, could not be used by the government as evidence in such litigation or in preparation for same. Manifestly congress did not, when it enacted section 3167, Revised Statutes, intend to defeat prosecutions and suits in court for which it has specifically provided.

Income returns filed with the department are public records of the department, and public records in the treasury department are of right available as evidence in litigation in court unless there is some statute making it unlawful to use them as such. (Winn v. Patterson, 9 Pet., 663, 677; Evanston v. Gunn, 99 U. S., 660; Williams v. Conger, 125 U. S., 397, 410; Iron Silver Min. Co. v. Campbell, 135 U. S., 286, 298; Oakes v. U. S., 174 U. S., 778; Texas, etc., Ry. Co. v Swarengen, 196 U. S., 51, 60.) As, therefore, the use of income returns or copies thereof in connection with litigation in court, where the United States government is interested in the result, is provided for by law, such returns or copies may be furnished for such use without a violation of the provisions of section 3167, Revised Statutes, as amended.

The following rules and regulations are therefore prescribed:

1. The original income return of an individual, partnership, corporation, association, joint-stock company, insurance company, or fiduciary, or a copy thereof, may be furnished by the commissioner of internal revenue to a United States attorney for use as evidence before a United States grand jury or in litigation in any court, where the United States is interested in the result, or for use in the preparation for such litigation, or to an attorney connected with the department of justice designated by the attorney general to handle such matters, if and when the attorney general states to the commissioner in writing that such income return or copy thereof is thus furnished, it must be limited in use to the purpose for which it is furnished, and is under no conditions to be made public except where publicity necessarily results from such use. In case the original return is necessary, it shall be placed in evidence by the commissioner of internal revenue or by some other officer or employee of the internal-revenue bureau designated by the commissioner for that purpose, and after it has been placed in evidence it shall be returned to the files in the office of the commissioner in Washington. An original return will be furnished only in exceptional cases, and then only when it is made to appear that the ends of justice may otherwise be defeated. Neither the original nor a copy of an income return desired for use in litigation in court where the United States government is not interested in the result and where such use might result in making public the information contained therein will be furnished, except as otherwise provided in the next succeeding paragraph.

2. A copy of an income return may be furnished by the commissioner of internal revenue to the person who made the return or to his duly constituted attorney, or, if the person is deceased, to his executor or administrator; or if the entity is in the hands of a receiver, trustee in bankruptcy, guardian, or similar legal custodian, to the receiver, trustee, or other similar custodian upon written application for same, accompanied by satisfactory
Income-Tax Department

evidence that the applicant comes within this provision. "The person who made the return" as herein used refers in the case of an individual return to the individual whose return is desired, and in the case of a return of a corporation, association, joint-stock company, insurance company, or fiduciary to the corporation, association, joint-stock company, or fiduciary, a copy of whose return is desired. A corporation may also designate by proper action of its board of directors the officer or individual to whom a copy of a return made by the corporation may be furnished, and upon sufficient evidence of such action and of the identity of the officer or individual, a copy may be furnished to such person. A copy of a partnership income return will be furnished to the partners only in case all the partners join in the request therefor, it matters not what particular partner or officer of the partnership made the return. If the partnership has been dissolved, the members surviving may be furnished a copy if all the members surviving join in the request.

3. All former regulations bearing on the subjects herein covered are hereby superseded.

II. GIVING TO STATE OFFICIALS ACCESS TO INCOME RETURNS OF CORPORATIONS, ASSOCIATIONS, JOINT-STOCK COMPANIES, AND INSURANCE COMPANIES

Section 2 of the tariff act of October 3, 1913, imposes an income tax on corporations, joint-stock companies or associations, and insurance companies, and requires them to file income returns. Paragraph G (d) of said section provides, among other things:

That the proper officers of any state imposing a general income tax may, upon the request of the governor thereof, have access to said returns, or to an abstract thereof showing the name and income of each such corporation, joint-stock company, association, or insurance company, at such times and in such manner as the secretary of the treasury may prescribe.

Title I of the revenue act of 1916 imposes an income tax on corporations, joint-stock companies or associations, and insurance companies, and requires them to file income returns. Section 14 (b) of said title provides, among other things:

That the proper officers of any state imposing a general income tax may, upon the request of the governor thereof, have access to said returns or to an abstract thereof, showing the name and income of each such corporation, joint-stock company or association, or insurance company, at such times and in such manner as the secretary of the treasury may prescribe.

Title II of the revenue act of 1917 imposes a war excess profits tax on corporations, joint-stock companies or associations, and insurance companies, and section 212 of said title provides:

That all administrative, special, and general provisions of law, including the laws in relation to the assessment, remission, collection, and refund of internal revenue taxes not heretofore specifically repealed, and not inconsistent with the provisions of this title, are hereby extended and made applicable to all the provisions of this title and to the tax herein imposed, and all provisions of title I of such act of September 8, 1916, as amended by this act relating to returns and payment of the tax therein imposed, including penalties, are hereby made applicable to the tax imposed by this title.

Title II of the revenue act of 1918 imposes an income tax on corporations, associations, joint-stock companies, and insurance companies, and requires them to file income returns. Section 257 of said title provides, among other things:

That the proper officers of any state imposing an income tax may, upon
The Journal of Accountancy

the request of the governor thereof, have access to the returns of any corporation, or to an abstract thereof showing the name and income of the corporation, at such times and in such manner as the secretary may prescribe.

Section 1 of title I of said revenue act of 1918 provides:

That when used in this act * * * the term "corporation" includes associations, joint-stock companies, and insurance companies.

Title III of the revenue act of 1918 imposes a war profits and excess profits tax on corporations, associations, joint-stock companies, and insurance companies, in addition to other taxes imposed by the act, and section 336 of said title provides:

That every corporation not exempt under section 304 shall make a return for the purposes of this title. Such returns shall be made, and the taxes imposed by this title shall be paid, at the same times and places, in the same manner, and subject to the same conditions as is provided in the case of returns and payment of income tax by corporations for the purposes of title II; and all the provisions of that title not inapplicable, including penalties, are hereby made applicable to the taxes imposed by this title.

Section 1000, title X, of the revenue act of 1918 imposes on corporations a special excise tax with respect to carrying on or doing business, and subdivision (d) of said section provides:

Section 257 shall apply to all returns filed with the commissioner for purposes of the tax imposed by this section.

Pursuant to the authority contained in these provisions of law or under laws heretofore enacted in substitution or amendment thereof and not inconsistent herewith the following rules and regulations are prescribed:

1. The proper officers of a state imposing an income tax are entitled as of right upon the request of its governor to have access to the income and profits tax returns of a corporation, association, joint-stock company, or insurance company, or to an abstract thereof, showing its name and income. Proper officers in this connection are only those officers of the state who are charged with the enforcement of the state income-tax law and who are to use the information gained by the access only in connection with such enforcement.

2. The request or application of the governor must be in writing signed by him under the seal of his state and must show:

(a) That the state imposes an income tax.
(b) The name and address of the corporation, association, joint-stock company, or insurance company making the returns to which access is desired.
(c) Why access is desired.
(d) The names and official positions of the officers designated to have the access.
(e) That such designated officers are charged with the enforcement of the state income-tax law.
(f) That the information to be gained by the access is to be used only in connection with such enforcement.

3. The request or application of the governor may be addressed either to the secretary of the treasury or to the commissioner of internal revenue, but should be transmitted to the commissioner, who will set a convenient time for the access to the returns (or to an abstract thereof as he may determine).

4. Access shall be given only in the office of the commissioner of internal revenue in Washington.

5. The officers designated by the governor will not be permitted to name another person or persons to examine the returns (or abstracts) for them.

6. The officers designated will be given access only to the returns of those corporations, associations, joint-stock companies, or insurance companies organized or doing business in their state.
Income-Tax Department

7. The officers designated may have access to lists furnished to supplement and become a part of the returns to which they are given access.

8. The proper officers, as defined in paragraph 1, may have access to the capital stock tax returns filed under the provisions of section 1000 of the revenue act of 1918 under the same conditions prescribed in the preceding paragraph for access to the income and profits tax returns of corporations, associations, joint-stock companies, and insurance companies. This right does not extend to the examination of capital stock tax returns filed pursuant to prior acts of congress.

9. All former regulations bearing on the subjects herein covered are hereby superseded.

III. Examination by a Stockholder of the Annual Income Returns of a Corporation Made Pursuant to Titles II and III and Section 1000, Title X, of the Revenue Act of 1918

Title II of the revenue act of 1918 imposes an income tax on corporations and requires them to file income returns. Section 257 of said title provides, among other things:

That all bona fide stockholders of record owning 1 per cent or more of the outstanding stock of any corporation shall, upon making request of the commissioner, be allowed to examine the annual income returns of such corporation and of its subsidiaries. Any stockholder who, pursuant to the provisions of this section, is allowed to examine the return of any corporation, and who makes known in any manner whatever not provided by law the amount or source of income, profits, losses, expenditures, or any particular thereof, set forth or disclosed in any such return, shall be guilty of a misdemeanor and be punished by a fine not exceeding $1,000, or by imprisonment not exceeding one year, or both.

Title III of the revenue act of 1918 imposes a war profits and excess profits tax on corporations, in addition to other taxes imposed by the act, and section 336 of said title provides:

That every corporation not exempt under section 304 shall make a return for the purposes of this title. Such returns shall be made, and the taxes imposed by this title shall be paid, at the same times and places, in the same manner, and subject to the same conditions, as is provided in the case of returns and taxes imposed by corporations for the purposes of title II; and all the provisions of that title not inapplicable, including penalties, are hereby made applicable to the taxes imposed by this title.

Section 1000, title X, of the revenue act of 1918 imposes on corporations a special excise tax with respect to carrying on or doing business, and subdivision (d) of said section provides:

Section 257 shall apply to all returns filed with the commissioner for purposes of the tax imposed by this section.

Pursuant to these provisions of law and any other laws that may be hereafter enacted in substitution or amendment thereof and not inconsistent herewith, a bona fide stockholder of record owning 1 per cent or more of the outstanding stock of a corporation shall be entitled as of right, upon making request of the commissioner of internal revenue, to examine the annual income returns of such corporation and of its subsidiaries made under titles II and III of the revenue act of 1918, and all returns of corporations filed for purposes of the tax imposed by section 1000, title X, of said act. His request for permission to examine such returns must be made in writing and must be in the form of an affidavit showing his address, the name of the corporation, the period of time covered by the return he desires to inspect, the amount of the corporation's outstanding capital stock, the number of shares owned by him, the date when he acquired them, and...
whether he has the beneficial as well as the record title to such shares. It must also show that he has not acquired his shares for the purpose of the examination of the income returns of the corporation. If he has acquired them for this purpose he is not a bona fide stockholder within the meaning of the statute. The application must be supported by satisfactory evidence showing that the applicant is a bona fide stockholder of record of the required amount of stock of the corporation. The supporting evidence may be partly in the form of a certificate signed by the president or vice-president of the corporation, and countersigned by the secretary under the corporate seal. Upon being satisfied from the evidence presented that the applicant has fully met these conditions the commissioner will grant the permission to examine the returns and set a convenient time for the examination in the office of the commissioner. This privilege is personal and will be granted only to the stockholder, who cannot delegate it to another.

All former regulations bearing on this subject are hereby superseded.

IV. Inspection of Returns in All Other Cases is Governed by Presidential Order and Regulations, to Which Reference is Made

(T. D. 2963, January 12, 1920)

Revenue act of 1918—Amendment of article 1568 of Regulations 45

Article 1568 of regulations 45 is hereby amended to read as follows:

Art. 1568. Determination of gain or loss from subsequent sale.—The new stock and securities received as described in the preceding article take the place of the old stock and securities. For the purpose, therefore, of ascertaining the gain derived or loss sustained from the subsequent sale of any stock of A or of the consolidated corporation, so received, the original cost to the taxpayer or the fair market value as of March 1, 1913, of the stock of B or A in respect of which the new stock was issued, less any untaxed distribution made to the taxpayer by A out of the former capital or surplus of B, or by the consolidated corporation out of the former capital or surplus of A or B, is the basis for determining the amount of such gain or loss. When securities of a single class are exchanged for new securities of the same total par value but of different classes, for purposes of determining profit or loss on subsequent sale of any of the new securities, the proportion of original cost (or value as of March 1, 1913) to be allocated to each class of new securities is that proportion which the market value of the particular class bears to the market value of all securities received on the date of the exchange. For example, if 100 shares of common stock, par value $100, are exchanged for 50 shares of preferred and 50 shares of common each of $100 par value, and the cost of the old stock was $250 per share, or $25,000, but the market value of the preferred on the date of exchange was $110 per share, or $5,500 for the 50 shares, and the market value of the common was $140 per share, or $22,000 for the 50 shares of common, one-fifth of the original cost, or $5,000, would be regarded as the cost of the preferred and four-fifths, or $20,000, as the cost of the common. Similarly, the cost after reorganization, merger, or consolidation of the assets of A or of the consolidated corporation is the sum of the cost (or the fair market value as of March 1, 1913) of the assets of A and of B for the purpose of ascertaining the gain or loss upon a subsequent sale. The new invested capital of A or of the consolidated corporation is to be determined as if A and B were rendering a consolidated return as affiliated corporations. See sections 240 and 326 of the statute and articles 631-638 and 864-869.
Students' Department

EDITED BY SEYMOUR WALTON
(ASSISTED BY H. A. FINNEY)

AMERICAN INSTITUTE EXAMINATION, NOVEMBER, 1919

In regard to the following attempt to present the correct solution to the questions asked in the examination held by the American Institute of Accountants in November, 1919, the reader is cautioned against accepting the solutions as official. They have not been seen by the examiners—still less endorsed by them.

ACCOUNTING THEORY AND PRACTICE

PART I

NOVEMBER 14, 1919, 9 A. M. TO 1 P. M.

Answer questions 1 and 3, and any three other questions

Question 1:

Spark Plug & Auto Supply, Inc., is the manufacturer of a patented spark plug and is also dealer in automobile supplies. From the following trial balance (as of October 31, 1919) and information prepare balance-sheet and profit and loss statements showing cost of manufacture of spark plugs and gross and net profit on sales:

Advertising .............................................. $26,450
Accounts receivable .................................$180,105
   " payable ........................................... $42,500
   Bills receivable ................................. 35,000
   " payable trade creditors ................... 22,700
   " " First National Bank ..................... 150,000
Bonds, 5% 1st mortgage ......................... 250,000
Building factory ................................... 225,000
Bad debts written off ............................ 7,850

Capital stock:
   Common fully paid
   Authorized $250,000
   Issued ........................................... 100,000

6% preferred:
   Authorized and issued ......................... 18,000
   300,000
   Dividend preferred stock ..................... 7,140
   Delivery expenses .............................. 9,250
   Directors' fees ................................ 2,500
   Discount on sales ............................. 12,200
   Freight: raw materials ....................... 12,050
   " automobile supplies ......................... 2,345
   Finished goods ................................. 34,320
   First National Bank current account ....... 51,850

145
<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>General expenses</td>
<td>14,770</td>
</tr>
<tr>
<td>Goods in process</td>
<td>13,250</td>
</tr>
<tr>
<td>Heat, light and power</td>
<td>22,200</td>
</tr>
<tr>
<td>Interest on bonds</td>
<td>9,375</td>
</tr>
<tr>
<td>Insurance and taxes: factory</td>
<td>17,400</td>
</tr>
<tr>
<td>Labor: productive</td>
<td>233,846</td>
</tr>
<tr>
<td>&quot; non-productive</td>
<td>99,444</td>
</tr>
<tr>
<td>Liberty bonds</td>
<td>105,000</td>
</tr>
<tr>
<td>Loose tools</td>
<td>15,270</td>
</tr>
<tr>
<td>Machinery and plant</td>
<td>165,090</td>
</tr>
<tr>
<td>Office furniture and fixtures</td>
<td>1,200</td>
</tr>
<tr>
<td>Payroll</td>
<td>4,278</td>
</tr>
<tr>
<td>Patent rights</td>
<td>30,000</td>
</tr>
<tr>
<td>Purchases: raw materials</td>
<td>450,960</td>
</tr>
<tr>
<td>&quot; automobile supplies</td>
<td>141,690</td>
</tr>
<tr>
<td>Repairs</td>
<td>14,050</td>
</tr>
<tr>
<td>Rent: warehouse</td>
<td>3,875</td>
</tr>
<tr>
<td>Reserve for depreciation: buildings</td>
<td>20,500</td>
</tr>
<tr>
<td>&quot; &quot; &quot; machinery</td>
<td>16,836</td>
</tr>
<tr>
<td>&quot; &quot; &quot; bad debts</td>
<td>8,000</td>
</tr>
<tr>
<td>Real estate: factory site</td>
<td>150,000</td>
</tr>
<tr>
<td>Shop supplies and expenses</td>
<td>15,560</td>
</tr>
<tr>
<td>Surplus</td>
<td>173,011</td>
</tr>
<tr>
<td>Sales: spark plugs</td>
<td>1,063,020</td>
</tr>
<tr>
<td>&quot; automobile supplies</td>
<td>137,595</td>
</tr>
<tr>
<td>Salaries: office and general</td>
<td>14,500</td>
</tr>
<tr>
<td>&quot; &quot; &quot; salesmen</td>
<td>34,600</td>
</tr>
<tr>
<td>Traveling expenses</td>
<td>22,300</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$2,288,440</strong></td>
</tr>
</tbody>
</table>

Inventories, November 1, 1918:

- Raw materials                         $ 14,500
- Automobile supplies                    22,450

Inventories, October 31, 1919:

- Raw materials                         27,300
- Automobile supplies                    19,200
- Finished goods                         50,400
- Goods in process                       17,205
- Loose tools                            10,500

Reserve for bad debts to be adjusted to 5% of open accounts.

Depreciation for the 12 months ended October 31, to be allowed as follows:

- Factory buildings, 2%.
- Machinery, 5%.
- Delivery equipment, 10%.
- Furniture and fixtures, $200.
- Disregard fractional parts of a dollar.
- Patent rights expire October 31, 1925.
- Advertising, $950.00 applies to next season.
- Taxes on factory buildings accrued, $1,400.00.
- First mortgage 5% gold bonds are a first charge on all the assets of the company.
- Interest payable quarterly on the first of February, May, August and November.
Students’ Department

Answer to Question 1:

The problem does not furnish any basis for the allocation of costs between spark plugs and automobile supplies, except that the company manufactures the former and only deals in the latter. All the manufacturing expense is therefore to be charged against the spark plugs, although part of the heat, light and power may be selling or office expense. The selling expenses might be apportioned between the two classes of sales, if proper data were available. The ratio between the sales of the two departments may be far from a proper basis for distributing the expense. The wording of the question would indicate that the gross and net profit is required on the total sales and not on each kind separately.

It is to be noted that the 1918 inventories of raw materials and of automobile supplies are included in the respective purchase accounts, while the other 1918 inventories are in separate accounts, which are not designated as inventories.

The credit to payroll, $4,278, is assumed to be accrued wages not yet due, although that entry is not usually made until the other adjusting entries are put on the books.

Profit and Loss Statement
Year ended October 31, 1919

Spark plugs:

Sales .................................................. $1,063,020

Cost of spark plugs made and sold:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goods in process, Nov. 1, 1918</td>
<td>$13,250</td>
</tr>
<tr>
<td>Raw material, inventory, Nov. 1, 1918</td>
<td>$14,500</td>
</tr>
<tr>
<td>Purchases</td>
<td>436,460</td>
</tr>
<tr>
<td>Freight</td>
<td>12,050</td>
</tr>
<tr>
<td></td>
<td>$493,010</td>
</tr>
<tr>
<td>Less inventory Oct. 31, 1919</td>
<td>27,300</td>
</tr>
<tr>
<td></td>
<td>435,710</td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Productive labor</td>
<td>233,846</td>
</tr>
<tr>
<td>Non-productive labor</td>
<td>99,444</td>
</tr>
<tr>
<td>Heat, light and power</td>
<td>22,200</td>
</tr>
<tr>
<td>Repairs</td>
<td>14,050</td>
</tr>
<tr>
<td>Shop supplies and expense</td>
<td>15,560</td>
</tr>
<tr>
<td>Factory insurance and taxes</td>
<td>18,800</td>
</tr>
<tr>
<td>Patents (1/7)</td>
<td>4,286</td>
</tr>
<tr>
<td>Loose tools</td>
<td>4,770</td>
</tr>
<tr>
<td>Depreciation, buildings</td>
<td>4,090</td>
</tr>
<tr>
<td>&quot; machinery and plant</td>
<td>7,412</td>
</tr>
<tr>
<td></td>
<td>190,612</td>
</tr>
<tr>
<td></td>
<td>$873,418</td>
</tr>
<tr>
<td>Less inventory goods in process</td>
<td>17,205</td>
</tr>
<tr>
<td></td>
<td>$856,213</td>
</tr>
</tbody>
</table>
Finished goods inventory Nov. 1, 1918 ........................................ 34,320

Finished goods inventory Oct. 31, 1919 ........................................ 59,400

Cost of spark plugs sold.............................................................. $840,133

Gross profit, spark plugs............................................................... $222,887

Automobile supplies:
Sales ................................................. 137,595
Inventory, Nov. 1, 1918................................................... 22,450
Purchases ................................................... 119,240
Freight .................................................. 2,345

$144,035

Less inventory Oct. 31, 1919 ........................................ 19,200

124,835

Gross profit automobile supplies.............................................. 12,760

Total gross profit ................................................................. $235,647

Selling expenses:
Rent warehouse .................................................. 3,875
Advertising .................................................. 25,500
Salesmen's salaries ........................................ 34,000
Traveling expense ........................................ 22,300
Delivery expense ........................................ 7,140
Depreciation delivery equipment ........................................ 925

94,340

Gross profit on sales........................................................... $141,307

General expense:
Salaries: office and general ..................................... 14,500
Directors' fees ........................................ 2,500
General expense ........................................ 14,770
Depreciation: furniture and fixtures .................................. 200

31,970

Operating profit................................................................. $109,337

Financing expense:
Bond interest ........................................ 12,500
Discount on sales ........................................ 12,200
Bad debts ................................................ 8,855

33,555

Net profit to surplus.......................................................... $ 75,782

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Students' Department

Surplus
Dividends paid on preferred.$ 18,000  Balance Nov. 1, 1918.....$173,011
Balance Oct. 31, 1919...... 230,793  Profits to Oct. 31, 1919..... 75,782

$248,793  Balance Nov. 1, 1919......$230,793

Balance-Sheet
October 31, 1919

Assets

<table>
<thead>
<tr>
<th>Fixed assets:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Buildings</td>
<td>$225,000</td>
</tr>
<tr>
<td>Less reserve</td>
<td>24,590</td>
</tr>
<tr>
<td>Machinery and plant</td>
<td>$165,090</td>
</tr>
<tr>
<td>Less reserve</td>
<td>24,248</td>
</tr>
<tr>
<td>Land: factory site</td>
<td>150,000</td>
</tr>
<tr>
<td>Delivery equipment</td>
<td>$9,250</td>
</tr>
<tr>
<td>Less reserve</td>
<td>925</td>
</tr>
<tr>
<td>Office furniture and fixtures</td>
<td>1,000</td>
</tr>
<tr>
<td>Patent rights</td>
<td>25,714</td>
</tr>
<tr>
<td>Investment: Liberty bonds</td>
<td>195,000</td>
</tr>
</tbody>
</table>

Active assets:

| Inventory: finished goods             | 50,400 |
| goods in process                      | 17,205 |
| raw material                          | 27,300 |
| auto supplies                         | 19,200 |
| loose tools                           | 10,500 |
| Bills receivable                      | 35,000  |
| Accounts receivable                   | 180,105 |
| First National Bank                   | 51,850  |

Deferred charges:

| Advertising                            | 950    |

$1,113,801

Liabilities

| Fixed liabilities:                     |     |
| Bonds                                  | 250,000 |

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The Journal of Accountancy

Active liabilities:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bills payable trade</td>
<td>22,700</td>
</tr>
<tr>
<td>&quot; bank</td>
<td>150,000</td>
</tr>
<tr>
<td>Accounts payable</td>
<td>42,500</td>
</tr>
<tr>
<td>Bond interest accrued</td>
<td>3,125</td>
</tr>
<tr>
<td>Wages accrued</td>
<td>4,278</td>
</tr>
<tr>
<td>Taxes accrued</td>
<td>1,400</td>
</tr>
</tbody>
</table>

Reserve, for bad debts............ 9,005

Capital and surplus:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital stock, common</td>
<td>100,000</td>
</tr>
<tr>
<td>&quot; preferred</td>
<td>300,000</td>
</tr>
<tr>
<td>Surplus</td>
<td>230,793</td>
</tr>
</tbody>
</table>

$1,113,801

Question 2:

The certificate of incorporation of the company referred to in the preceding question provides for the redemption of preferred stock "out of surplus profits," $30,000, to be redeemed November 1, 1919, and $30,000, yearly thereafter. The stock redeemed in 1919 is to be purchased at 105 and accrued dividends, in 1920 at 110, and so on, the 1928 redemption being at 150.

Assuming that purchases of stock are made in accordance with the above requirements, and that the directors take the necessary steps for the cancellation of the issue, explain how the various transactions should be recorded in the books of the company and illustrate your answer by journal entries.

How would you show the accounts in the balance-sheet at any time during the redemption period?

Answer to Question 2:

The premium on the stock redeemed is a financial loss to the company, but it is not an operating loss to be charged in the profit and loss account of any one year. It is a charge against surplus, and should be made when closing the books on October 31st of each year. The entry would be in 1919:

Preferred stock ........................................... $30,000.00
Surplus .................................................. 1,500.00

Holders of redeemed stock..................... $31,500.00

To carry out the action of the board of directors redeeming preferred stock.

There could also be an entry as follows:

Surplus .................................................. $30,000.00
Appropriated surplus .......................... $30,000.00

To show appropriation of proceeds of surplus to redemption of stock.

It is assumed that there would be some provision designating which stock was to be redeemed, probably 10 per cent of each stockholder's original holdings. Otherwise it might be impossible to get the stock at 105.
Students' Department

The provision for the accrued dividend seems to have been made already, since the full year's dividend has been charged.

When the holders of the redeemed stock are paid, their account will be charged; but as that is not done until after October 31st, it does not affect the balance-sheet.

All the changes in the balance-sheet will be on the credit side. Capital stock preferred will be reduced $30,000.00; free surplus will be reduced $1,500.00. To offset these there would be a new account of redeemed stock $31,500.00. The surplus account would be divided as follows:

<table>
<thead>
<tr>
<th>Surplus:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Appropriated to redeem preferred stock</td>
<td>$30,000.00</td>
</tr>
<tr>
<td>Free</td>
<td>199,293.00</td>
</tr>
<tr>
<td></td>
<td>$229,293.00</td>
</tr>
</tbody>
</table>

The only question that can be raised is as to whether or not the premium shall be averaged, instead of being charged off as it is paid. The total premium in the ten years would amount to $82,500.00 and the annual average would be $8,250.00. The objections to this plan are that the annual increase in the premium is evidently intended to make the burden proportionate to the surplus, which it is naturally expected will also increase; that there is no absolute certainty that the company will make enough profit to permit the redemption of the stock regularly every year, and the average may be destroyed; and that the premium is in reality an extra dividend, and dividends are not charged to surplus until they are declared payable.

It is hardly worth while to consider a claim that might be made that the premium is a special dividend of 5 per cent declared each year on all the outstanding stock—in other words that the stock is actually preferred at 11 per cent, 6 per cent payable in cash on all the outstanding stock, an additional 5 per cent in cash on $30,000 of the stock each year, and that 5 per cent is to be credited to accrued dividends not due on the unredeemed stock. This would set up a large accrued liability which did not exist and would not materialize until the directors had taken appropriate action each year.

Question 3:

In Mr. Jones' private ledger he keeps accounts with each investment he makes, one of which is an investment of 1,000 shares (par value $100) of the A. B. Company, which he acquired in July, 1914, for $85,000. After this date and up to December 31, 1918, he makes further purchases and sales of this stock. A certified public accountant called in to prepare Mr. Jones' income-tax return for 1918 finds that these and other transactions have been written up in the following manner, no effort to show the profit on the sale of 1,000 shares on June 1, 1918, having been attempted:

<table>
<thead>
<tr>
<th>Investment A. B. Company Account</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 1/14. 1,000 shares purchased</td>
<td>$85,000</td>
<td></td>
</tr>
<tr>
<td>Dec. 31/14. Entry to carry this stock at par</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>May 31/15. Purchased 1,500 shares at par</td>
<td>150,000</td>
<td></td>
</tr>
<tr>
<td>Nov. 30/15. Sold 300 shares at 125</td>
<td></td>
<td>$37,500</td>
</tr>
<tr>
<td>Dec. 31/15. Profit and loss—profit on sale of 300 shares</td>
<td>7,500</td>
<td></td>
</tr>
</tbody>
</table>

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July 1/16. Stock dividend of 50% on 2,200 shares declared from profits accumulated prior to March 1, 1913. ........................................ 110,000
Feb. 28/17. Sold 700 shares @ 110. .................................. 77,000
Dec. 31/17. Profit and loss, profit made on sale of 700 shares ......................................................... 7,000
June 1/18. Sold 1,000 shares @ 125. .............................. 125,000

Rewrite this entire account to show how it should have been kept in order to show the actual profit on each sale, and also calculate the actual profit on the last sale of 1,000 shares. What is the book value of the total shares on hand December 31, 1918?

Answer to Question 3:

If the shares of stock of the A. B. Company, purchased and sold by Mr. Jones at various times, could in each case be identified—that is, if the shares represented by each purchase were kept distinct from the shares involved in each other purchase, by a record of certificate number, by marks upon the certificates or by some other method—it would be necessary to use a separate account for each purchase, since each lot of shares would constitute a distinct and separate unit of property for income-tax purposes. Any one of such units could be sold at any time by Mr. Jones without interfering with the other units, and he would be required to report the taxable gain or deductible loss for that particular property, consisting of the difference between its cost and selling price. For example, in making his sale of 300 shares on November 30, 1915, he might sell 300 of the shares purchased at 85, in which case he would make a profit of $12,000, or he might sell 300 of the shares purchased at par, in which case he would make a profit of $7,500. Assuming, however, that Mr. Jones is unable to identify the particular shares purchased at any time, which would be the result if he obtained a single certificate after his purchase of May 31, 1915, to represent his 2,500 shares then owned, the accounts would be kept as follows, based upon the presumption that the shares sold at any time were the shares then owned which had been first purchased, and that any shares remaining unsold were the shares which had been last purchased.

Stock of A. B. Company

<table>
<thead>
<tr>
<th>Date</th>
<th>Description</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 1, 1914</td>
<td>1,000 shares purchased at 85...</td>
<td>$ 85,000.00</td>
<td></td>
</tr>
<tr>
<td>May 31, 1915</td>
<td>1,500 shares purchased at 100.</td>
<td>150,000.00</td>
<td></td>
</tr>
<tr>
<td>Nov. 30, 1915</td>
<td>800 shares sold at 125, cost 85.</td>
<td></td>
<td>$ 25,500.00</td>
</tr>
<tr>
<td></td>
<td>(Credit profit and loss, $15,000)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>July 1, 1916</td>
<td>Stock dividend of 50%—1,100 shares. (Cost of remaining 700 shares purchased at 85, or $59,500, now represents cost of 1,050 shares, or $56.67 per share. Cost of 1,500 shares purchased at par now represents cost of 2,250 shares, or $66.67 per share.)</td>
<td>$ 25,500.00</td>
<td></td>
</tr>
</tbody>
</table>
### Students' Department

**Dec. 31, 1916.** Balance, cost of remaining shares:

<table>
<thead>
<tr>
<th>Shares</th>
<th>Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,050 shares at $66.67</td>
<td>$69,500.00</td>
</tr>
<tr>
<td>2,250 shares at 66.67</td>
<td>150,000.00</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$209,500.00</strong></td>
</tr>
</tbody>
</table>

**Jan. 1, 1917.** Balance forward:

<table>
<thead>
<tr>
<th>January 1, 1917</th>
<th>Share Forward</th>
</tr>
</thead>
<tbody>
<tr>
<td>700 shares sold at 110, cost $66.67</td>
<td><strong>$39,666.67</strong></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$209,500.00</strong></td>
</tr>
</tbody>
</table>

**Feb. 28, 1917.** 700 shares sold at 110, cost $66.67

**June 1, 1918.** 1,000 shares sold at 125, cost $86.67

**Dec. 31, 1918.** Balance, cost of remaining shares:

<table>
<thead>
<tr>
<th>Shares</th>
<th>Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,250 shares at $86.67</td>
<td>$103,166.66</td>
</tr>
<tr>
<td>350 shares at 56.67</td>
<td>19,833.33</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$123,000.00</strong></td>
</tr>
</tbody>
</table>

The entry with reference to the last sale made on June 1, 1918, and the computation of profits thereon, are based upon a strict literal application of the rule stated by the treasury department as follows: "The stock sold shall be charged against the earliest purchases of such stock." It is true that Mr. Jones held on that date 350 shares which he had acquired on July 1, 1916, as a result of the stock dividend upon the 700 shares of his first purchase in 1914. It might therefore be contended that these 350 shares were held by Mr. Jones as the result of his first purchase, and therefore that any sale should be charged against this stock in priority to the stock purchased on May 31, 1915. On the other hand, on June 1, 1918, Mr. Jones owned 1,500 shares, which were purchased at a date prior to the date when he acquired the 350 shares received as dividend. It seems to follow that the sale on June 1, 1918, should be charged against this prior purchase, rather than against the stock subsequently received by reason of the stock dividend, even though the stock dividend was in part paid upon shares purchased at a still earlier date. Mr. Jones is also entitled to claim the benefit which he obtains by this interpretation until the treasury department changes its rulings. If this sale were charged against the 350 stock dividend shares, the taxable income of Mr. Jones would be $3,500 greater than it is according to the method used. (Answered by Kixmiller & Baar, counsel for Commerce Clearing House.)

**Question 4:**

Discuss the treatment of expenditures for (I) ordinary repairs and (II) replacements in their relation to capital expenditures, profit and loss and reserve for depreciation.

**Answer to Question 4:**

(I) Managers, superintendents and foremen are naturally interested in
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keeping down operating expenses for which they are responsible. Their interest lies in charging repairs, which are operating expenses, to the asset account of machinery, etc., charges to which are capital expenditures. If allowed to do this, they are unduly inflating the assets with items which do not increase any asset values and are equally inflating the profits by the omission of operating costs.

Where ordinary repairs are nearly uniform in different periods they may be charged as operating cost as they occur. Usually they are not uniform, and should be averaged by a uniform charge to operating and a credit to reserve for repairs. Actual expenditures are charged to the reserve. Sometimes the reserve for depreciation is made large enough to include repairs, but it is better to have a separate reserve account.

(II) When an asset which is scrapped as a unit is replaced, the proper entry is to credit its original value to the asset account and to charge cash for the scrap value realized, if any, reserve for depreciation with the amount that has been credited to it for this particular asset, and surplus for the difference, if any, unless the plan of averaging depreciation is adopted. The cost of the new asset is charged to the asset account. In this way any increase or decrease in the value of the new asset as compared with the old one is taken up as a capital expenditure or saving.

When parts of an asset are replaced from time to time, the asset is to that extent virtually as good as new—that is, the depreciation of that part of the asset has been offset, and the cost of replacement should be charged to depreciation reserve. If the asset is permanently improved, a portion of the cost should be charged to the asset account as a capital expenditure. The only profit and loss entry would occur when the reserve for depreciation was set up.

Question 5:

A corporation carries on its books an account with patents it has acquired from time to time by outright purchase during a period of ten years. They are still carried at original cost and it is decided to determine their present value, based upon the expiration of the life of the patents. Describe how you would proceed accurately to secure this result.

Answer to Question 5:

The life of a patent is 17 years; therefore the date at which it will lose its value is accurately known. It is a wasting asset, and is considered to lose value each year in proportion to the number of years it still has to run, or, to be accurate, the number of months. The amount paid for each patent is divided by the number of years or months that it then had of remaining life to determine the rate of wastage. This rate of wastage is multiplied by the years or months elapsed between the date of purchase and the present date, the product being credited to the patent account and charged to surplus. In closing the books each year in the future the amount of wastage on the patents is charged as an operating expense.

In ordinary circumstances the possession of exclusive rights under the patents gives a business the opportunity to establish a valuable goodwill.
Students' Department

If the amounts paid for the patents are very large, it may be successfully claimed that part of their cost was incurred in paying for this goodwill. If that is so, the whole of the cost of the patents need not be written off during their life, but a portion may be left as goodwill.

Question 6:
A wholesale and retail company, which also manufactures most of the goods sold by it, determines through its cost system in the factory the cost of manufacture and proposes to bill its wholesale department for all goods manufactured at cost plus 10%. What effect will such procedure have on statements issued by this company?

Answer to Question 6:
This procedure would mean that the wholesale department was apparently paying 10% too much for the goods and that its profits were correspondingly reduced. Both manufacturing cost and selling expense would be thrown out of proportion in relation to net sales. The total profits of the company would not be affected as far as the goods made and sold during the year were concerned, but the profits would be reduced by an amount equal to one-eleventh of the goods on hand at the beginning of the year, and would be increased to the extent of the same proportion of the goods on hand at the end of the year, if the inventories were taken at the prices billed to the wholesale department.

A business cannot make a profit by manufacturing goods. It is necessary to sell them before any profit can be made; therefore it is not scientific to allow the factory any profit on the goods it makes.

Question 7:
State briefly the reasons advanced against including interest on owned capital in manufacturing costs.

Answer to Question 7:
It is assumed that this question refers only to the capital that is invested in the factory, since, as far as we know, it has never been claimed that any interest should be added to manufacturing costs except that calculated on the value of the fixed assets necessary to manufacture the product.

Manufacturers do not invest in land, buildings and machinery for the sake of earning interest. They expect that the use of these fixed assets will produce goods the sale of which will result in profits. If the expected profits consisted merely of interest there might be some foundation for the claim that interest was part of the cost. The profits cover much more than interest, such as the element of risk, the personal business ability of the proprietors or their representatives, taxes on capital and earnings and usually a further element of extra profit in prosperous years to provide against a decrease in normal returns in poor years.

Interest should not be considered an operating cost at all. It is the business of capital to furnish all the funds necessary to carry on an enterprise. If there is not ready money enough supplied by the capital of the proprietors it is necessary to call in others to supply the lack. Therefore,
capital offers investors inducements to advance the necessary funds. The inducement is larger or smaller according to the security that is offered, whether on short unsecured notes or on long-term bonds amply secured by real estate. The raising of this money is entirely the concern of capital and not of the manufacturing department of the business.

The impossibility of fixing a rate which can be called pure interest is another objection. All interest payments are influenced to a certain extent by the risk incurred in even the best secured loans. There is no such thing as a natural rate of interest, since the element of risk is always present and must always be covered.

If it is claimed that interest actually paid by the company will furnish the rate, an insuperable difficulty arises when more than one rate is paid. The interest paid may be at one rate on preferred stock, another on long-time bonds and a third on short-time notes.

The greatest objection of all is that the inclusion of interest on the value of factory fixed assets would be illogical unless interest is also included on account of the capital tied up in material and labor paid for in many cases long before the goods are finished. If it costs interest to carry fixed assets, interest certainly would be required also to carry all the other manufacturing expense until the goods are turned over to the selling department. Even then interest would not stop, because it is still necessary to carry large sums locked up in goods on hand and in accounts receivable, until actual cash is realized. Interest would then be a selling cost also. Unless a concern were a heavy borrower, the result would be that its charges to manufacturing cost and to selling expense and credits to interest would result in showing a large net earning from interest, when it may not have received a single dollar of actual interest.

**Inventory at Cost or Market**

*Editor, Students' Department:*

*Sir:* Should an inventory of raw material used in a printing plant be taken at its actual cost or at market value? I have seen articles from time to time in *The Journal of Accountancy* advising cost or market whichever is lower, although I am inclined to believe this is meant to cover mercantile establishments only, and would not apply to inventories of raw material in a manufacturing plant the selling price of whose finished product is based on actual costs. Am I correct in this assumption?

Your valuable advice will be greatly appreciated. 

Yours truly, 

H. B. M.

Harrisburg, Pennsylvania.

I have always taken the ground that the rule in regard to valuation of inventories at whichever price is lower, cost or market, did not apply when the selling price was not affected by a drop in the market.

If I am making flour, and wheat falls, I shall have to reduce the price of my flour. But if I am making a breakfast food my price is virtually stable; therefore I shall make a smaller profit on the produce made from my
inventory of wheat than I would have made if I had bought less wheat. But that is a question to be settled when the sales are made, not when the inventory is taken.

In your case I should certainly take the inventory at cost without any regard to market conditions, since the selling price is based on actual cost and is not affected by the market price of raw materials.

Because a profit is less than it might have been does not make it a partial loss at one time and a greater profit at another, as would be the case if you valued inventory at less than cost. When sales are made the next month you would register a profit that you did not make, to offset the apparent loss at the last closing which was not then realized and never would be realized as a loss.

The effect on the income tax is not considered. If the inventory is taken at market value the tax this year would be reduced, while that for next year would be correspondingly increased.

**CAPITALIZATION OF GOODWILL**

*Editor, Students’ Department:*

Sir: I trust that I am not exceeding my privilege as a subscriber in asking you the following question:

A corporation organized prior to March 1, 1913, has a capital of $200,000 and a surplus at the present time of $500,000. Its average earnings have exceeded 20% annually on the capital invested. The business is not of a fluctuating nature, but steadily increases in both volume and percentage of earnings. It seems apparent that the corporation has a goodwill equal in value to the capital stock.

Can this goodwill be set up as an asset on the books and stock be issued in an equal amount and distributed to the present stockholders without causing them to pay taxes thereon?

Or would it be necessary to distribute the total surplus created from earnings before this could be done?

Or would it be possible to set up goodwill as an asset on the books of the corporation and provide a special reserve of equal amount and be able to use 25% of the amount as capital?

Yours truly,

A. C. K.

Evansville, Indiana.

The goodwill cannot be put on the books at all as you propose. Dicksee, the English authority, says: “The only excuse for the insertion of such an item as goodwill in accounts is that such an amount has actually been paid by the present proprietor for the goodwill of a business.” This opinion has been universally concurred in by all accountants in this country as well as in Great Britain.

The reason for this is that the plan falsifies the profits and leads to a still further expansion if logically carried out. The only offsetting entry would be a credit to surplus. If it is desired to increase the capital stock, it can then be done by a stock dividend.

In the case in point, if it is considered that the accumulation in a given
time of a surplus of $500,000 is a justification for writing into the accounts a goodwill of $200,000, the surplus will become $700,000. But if $500,000 justifies a 40% goodwill, or $200,000, a surplus of $700,000 would justify a goodwill of $250,000, raising the surplus to $780,000, necessitating the raising of the goodwill to $312,000, and so on.

If the corporation should combine with others in a new company, it could and, of course, would demand a recognition of its goodwill. If that were agreed to be worth $200,000 the corporation would receive from the new company $900,000 in payment for its business to cover its capital stock of $200,000 and surplus of $700,000. The new company, having paid for the goodwill, is entitled to carry it as an asset for its cost, $200,000, and this is the first time it can legitimately appear as an asset on any books. Of course, it can at the same time be put into the accounts of the original corporation by an offsetting credit to surplus in recognition of and preparation for the sale. It is a credit to surplus and not to capital, because it is an increase in the net worth of the business, which now becomes a real profit by realization through the sale.

Goodwill is a fixed asset and as such cannot be written up; therefore the new company, however prosperous, cannot increase the amount beyond its cost.

**STOCK RECORD AT BRANCHES**

*S*, I would appreciate your advice on the following problem, which has come up in our business:

We wish to maintain a stock record at all branches on finished products and raw materials and at the same time have check on them at the home office. General books, including expense ledgers, are handled in home office, branches having only sales ledgers at present. All finished products and raw materials are billed to branches at cost prices; but as we do not wish various stock clerks to know cost prices, I am at loss just how to handle the matter.

J. D. G.

Freeport, Illinois.

As I understand your question you wish to bill the goods to the branches in such a way that you will always know the quantities and the cost of the shipments.

You can keep track of the quantities in various ways. If there are many items the best way is to have a card system for each branch. This requires a card for each kind of goods, with columns for quantity sent to, sold by and on hand at the branch. It hardly seems worth while to keep such an elaborate system of cards.

If you bill at cost there is no way to prevent any one at the branch from forming the opinion that the prices are cost. The best way is to bill at either selling prices or at some figure so much higher than cost as to make it evident that it cannot be cost. By always adding the same percentage to actual cost it is easy to reduce your conventional price to cost.

It does not make a particle of difference at what price you bill a branch because, of course, you credit all shipments to branches to “branch sales”
Students' Department

and not to your regular sales account. The only time when cost is necessary
is in pricing the inventory at the branch, and, as that is done on the home
office books, the branch knows nothing about it.

Averaging Cost

Editor, Students' Department:

Sir: I shall be greatly obliged if you will give this question your con-
sideration and give me your answer at your earliest convenience:

Over a separating table which costs $10.00 an hour to operate, there pass
ten tons of sand. This sand contains four different minerals, every ten tons
containing one ton mineral A, two tons mineral B, three tons mineral C and
four tons mineral D. These various minerals are separated by the table.
The question is: Shall the cost of operating the table for one hour be
divided by the ten tons produced, giving mineral A produced a cost of $1.00,
mineral B $2.00, mineral C $3.00, mineral D $4.00, or shall the cost of the
one ton of mineral A be $ of $10.00, two tons mineral B $ of $10.00, three
tons mineral C $ of $10.00, and four tons D $ of $10.00?
Thanking you for your consideration of this problem, I remain,
Very truly yours,

Niagara Falls, New York.

R. S. T.

As the cost of separation must be in proportion to the number of tons
handled, my opinion is that each class of sand should be charged with the
proportion of cost that its tonnage bore to the total tonnage. In this case
A would be charged $1.00, B $2.00, C $3.00 and D $4.00. It is hardly possible
that it would cost no more to separate D's four tons than it does A's one ton.

Suppose different lots varied, as I should think they would, and the result
of one was: A 1, B 1, C 2 and D 6. If each is charged $ of the cost, this
lot would show twice the normal per ton cost for B and 1½ times for C,
while D's cost would be only ½. This does not seem logical. It would make
it difficult to ascertain standard costs for the different grades.

Enos Spencer

Enos Spencer, of Louisville, Kentucky, died suddenly January 17, 1920.
Mr. Spencer was one of the oldest and best-known members of the American
Institute of Accountants, and had always been active in conventions and other
matters concerned with the progress of the profession to which he belonged.
For many years he had been not only a practising accountant, but also an
instructor.
North Carolina Society of Public Accountants

The North Carolina Society of Public Accountants, Inc., announces that it has received a charter and that the officers of the society are: president, Charles N. Goodno; vice-president, J. B. McCabe; secretary and treasurer, George E. Wood.

Klein, Hinds & Finke announce that James E. Tallent, D. C. Eggleston and William Steinberg have been admitted to partnership in the firm. The firm also announce the opening of a branch office at 11 Pemberton square, Boston, Massachusetts.

Reuben Hirsch and M. Albert Welt announce the formation of a partnership under the firm name of Hirsch-Welt & Co., with offices at 299 Broadway, New York, and 128 Broad street, Elizabeth, New Jersey.

James O. Sully announces that he has formed a partnership with E. G. Wunner, under the firm name of James O. Sully & Co., with offices in Merchants National Bank building, San Francisco, California.

Marwick, Mitchell & Co. announce the opening of an office in the H. W. Hellman building, Los Angeles, California, under the management of Walter C. Wright and Willis H. Brown.

Webb, Read & Co. and George A. Touche & Co. announce that their practices in Canada have been amalgamated and will be carried on under the firm name of George A. Touche & Co.

Rudolph Holde and Nathaniel W. Gropper announce the formation of a partnership under the firm name of Holde, Gropper & Co., with offices at 299 Broadway, New York.

Touche, Niven & Co. announce the opening of a branch office in the Society for Savings building, Cleveland, Ohio, in charge of Henry E. Mendes.

Touche, Niven & Co. announce the admission to partnership of Charles R. Whitworth, Henry E. Mendes and Francis J. Clowes.

Covington, Sauer & Scarborough announce the opening of offices at 409-410 Woodward building, Birmingham, Alabama.

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