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Book Reviews

INTRODUCTION TO GOVERNMENTAL ACCOUNTING, by LLOYD MOREY. *John Wiley & Sons.* 314 pages. 1936.

The fact that Professor Morey finds it necessary to write a second edition—a third printing—of his original work, published in 1927, and the willingness of the publishers to issue it are encouraging. It indicates the progress which has been made recently in this branch of accounting and also that the public takes sufficient interest to warrant the expense of a new edition.

Professor Morey's original book was reviewed in THE JOURNAL OF ACCOUNTANCY for January, 1928, and it is so well known as a standard work on the subject that is is unnecessary to dwell on the original plan.

The first question which presents itself to the enquiring mind on taking up this volume is: "What are governmental accounts?" Curiously enough, no definition appears in *Accounting Terminology* or in the tentative revision thereof which is now in private circulation. The expression is taken to be self-explanatory, but it includes a wide range, running from the accounts of a national government to those of a minute village and covers an unusual breadth of subjects including the treatment of "funds," the many complications arising in bonded indebtedness, the operation of public utilities and many others. In the present case the interest is directed especially to the accounts of states, counties and manicipalities.

The author has in mind two main purposes: first, to call attention to the many differences which exist—although often overlooked—between governmental and commercial accounting: second, to discuss the principles involved in these differences and to describe the methods of recording which are, or should be, adopted. While many examples are given, the author makes no attempt to tie the reader down to any iron-clad forms.

Probably the most striking difference between governmental and commercial accounting is the fact that—except in some subsidiary accounts such as those for public utilities—governmental accounts are not concerned with profits, while in commercial accounting each succeeding year finds more emphasis placed on the statement of profit and loss showing the amount of, the source of and the exact period in which are derived the earnings.

While the importance of "profits" is wiped out or diminished, the importance of the budget is correspondingly increased, and one of the principal purposes of governmental accounting is to show a comparison of the adopted budget with the accomplished results.

Other principal differences occur in the balance-sheet, for the major fixed assets of a government are not convertible into cash is as generally the case with commercial ventures. Such items as street paving, sewers, etc. have no fair market value—they are not salable, their present value is not important—yet it is necessary to keep record of them to show what has been done with taxpayers' money. As the author states, "problems of governmental accounting are primarily problems of governmental administration," therefore he, very wisely, "deals chiefly with principles rather than with details of form or procedure."

Another distinguishing characteristic is the fact that, speaking generally, all governmental transactions are "analysed and classified throughout by funds" and, as a result a complete set of such accounts consists of the accounts of a number of funds. Still another characteristic is the practice of controlling expenditures through a budget.

These matters are dealt with at length in the first five chapters of the volume; after which the various practical details such as revenues, expenditures, cash and social funds of various kinds are described. Finally there is a discussion of the methods of dealing with fixed assets and liabilities and the preparation of a governmental balance-sheet and the preparation of reports. Numerous illustrative statements are given and the transactions shown therein are brought into a final balance-sheet, entitled "balance-sheet—all funds," which is, perhaps, a preferable title to the expression "consolidated balance-sheet," for the combined governmental balance-sheet differs materially in form and in meaning from a commercial statement bearing the same name.

The general principles laid down in the first edition of 1927 remain the only important changes in the edition of 1932 relating to the accounts of trust funds. Professor Morey's position as vice-president of the National Committee on Municipal Accounting and as chairman of the American Institute's committee on governmental accounting has afforded him unusual opportunities to study the varying phases of governmental accounting and in this new edition of his work he has made numerous revisions so that the result may be taken to reflect the best and most modern theories and practices.

It is impossible to describe in detail these numerous changes—they are the result of greater uniformity of modern practice, of wise discussion by those engaged in governmental accounting, of a ripened judgment and of the preparation of a "terminology of municipal accounting."

Among the principal of these additions is an extended treatment of expendable revenue funds and of the treatment of property accounts, which are now dealt with under the head "fixed assets." The consolidated balance-sheet has become the governmental balance-sheet and useful examples and forms have been added to the chapter on reports.

The number of problems, each of which is based on a specified chapter of the book, has been increased to 58, and where necessary the problems have been revised to bring them into accordance with the practice of today.

An excellent bibliography has been added.

In view of the importance of the subject, of the rapid crystallization of ideas regarding it and of the acknowledged authority of the author it is difficult to see how any accountant interested in municipal or other governmental accounting can afford to remain without a copy of this book in his library.

WALTER MUCKLOW.

STABILIZED ACCOUNTING, by HENRY WHITCOMB SWEENEY. *Harper & Brothers*, New York. Cloth. 219 pages. 1936.

When a work on accounting, and on a most technical and abstruse variety of accounting, is given a place in the recommended list of the "Book of the Month" club, it is surely a phenomenon, startling, breathtaking, unique. Never before has a treatise on that subject been so honored.

This time the honor is well-bestowed. The topic, which refers to adjusting accounting technique so as to show correct results in spite of currency fluctuation, is extremely timely. The treatment is scholarly and shows an intimate and intelligent acquaintance with a wide field of generally neglected literature in French and German.

The book begins with an obvious, but, alas, not an unneeded, exposé of the meaninglessness of balance-sheets and income statements in time of inflation. Then comes the technique for producing a truthful picture in such a situation. It should be noted that this technique does not alter the ledger accounts as customarily constructed but supplies the correcting information through an additional self-balancing account which is entitled "stabilization adjustments." With this information readily available in a permanent record, it is possible to modify the conventional balance-sheet and income statement so as to present a true picture of the profit actually made, showing the effect of currency fluctuation. Thus, if an article which cost $100, when the dollar had a given value, is sold for $150 when the value of the dollar has shrunk 50 per cent, the accounts would show not a gain of $50, but a loss of fifty of the then current dollars.

Thus, the author states, the accounts "measure substance instead of just form" (p. 194). For making these adjustments, he prefers the use of a general price index such as that compiled by Carl Snyder.

While a preference is expressed for valuation based on replacement, rather than original cost, the method proposed is in no way linked to one base rather than another. It is applicable whether one prefers cost, replacement value or the hybrid cost-or-market whichever is lower. All that the system proposes is that if cost is preferred, that cost shall be expressed in comparable units—units representing present purchasing power.

This seems to have been misunderstood by some reviewers, who infer that the method of stabilizing at current price levels means valuing the plant at replacement cost. But Mr. Sweeney makes the matter clear in the following statement:

"If an asset cost $1,000 when the general price level was 125, then the reëxpression of that original cost on the basis of a later general index of 150 is $1,200. The *market* value of the asset at the later date might be any amount from zero to infinity. There is not much likelihood of its also being $1,200" (p. 203).

The detailed application of the method is illustrated, using the statements of actual corporations (with disguised names) in diverse lines of business. These are a public utility, a woollen mill and a factoring corporation. Further diversity is shown by so choosing dates that in one case the price level was the same at the end as at the beginning of the year; in another it was higher; in the third, lower.

In each instance there is shown a marked divergence between the amount of profits according to conventional accounting and the profits on a stabilized basis. By a detailed statement of the actual expense in obtaining these corrected figures, the author shows that the cost is not excessive, considerably less than that paid for the regular audit of the accounts. While no money value can be placed on the information gained, he considers it far outweighs the expense involved. Thus, in the case of the public utility, the stabilized statements showed, in contrast to the unstabilized, a deficit instead of an ample surplus, a net current income of only one-third of the book figure, and that the rates charged consumers were too low to cover expenses,

"In other words, the unstabilized book figures advised the continuance of present policies and the maintenance of present conditions. But the stabilized figures advised immediate and drastic change" (p. 103).

There are matters of detail open to question and criticism. But the method proposed by Mr. Sweeney has distinct advantages over those advocated during inflation in Germany, when stabilization in some form was imperative. But although the situation is not so compelling here and now, the matter is one which accountants should not cavalierly dismiss on the ground that it is not "orthodox accounting." The profession should give careful attention to this work, and defer criticism of minor and unessential details until its main thesis has been grasped. It is well worth serious study.

HENRY RAND HATFIELD.

HOW TO EVALUATE FINANCIAL STATEMENTS, by ALEXANDER WALL. *Harper Brothers,* New York. 319 pages. 1936.

How to Evaluate Financial Statements is written primarily for the credit men or credit analyst in a bank or a commercial house. It will be interesting to accountants chiefly because of the method of approach to financial statements.

The first 146 pages are devoted to a discussion of the processes, which are illustrated by actual cases in the second part. The identity of the concern is obscured by showing dollar figures differing from actual, which are, however, presented in the same ratio as those of the company which is being studied.

"Common size statements," in which the various items in the balance-sheet are reduced to percentages of the total, are prepared in the first instance. In this way comparisons may readily be made of an individual company's figures between years and with other companies in the same business. Incidentally the whole stress seems to be put on proportion and practically no consideration is given to volume.

Instead of the "current" and "profit to sales" ratios with which accountants are most familiar, Mr. Wall develops nine ratios from financial statements: three directly from the balance-sheet figures, four relating sales to balance-sheet figures and two relating profits to sales and to net worth. He then proceeds to assign various weights to the different ratios.

The book should not perhaps be recommended to the junior accountant not thoroughly grounded in accounting theory. In the opinion of the author, a statement of surplus should be built up on incomplete data and any unlocated difference scrutinized with concern. The accountant would, of course, ask the comptroller for a surplus statement in the first place. Again, it is recommended that the depreciation reserve be carried on the liability side of the balance-sheet on the grounds that machines must be replaced; "the nearer depreciation comes to actual final application the nearer we approach to a forced debt rise." The accountant will wholeheartedly agree with the author's recommendations with regard to the natural business year.

D. F. MORLAND.