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Correspondence: “Some Phases of Capital Stock”

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"Some Phases of Capital Stock"

Editor, The Journal of Accountancy:

SIR: A communication from A. R. M. Boyle, C. A., appearing in the July issue of THE JOURNAL OF ACCOUNTANCY attacks rather vigorously the writer's opinion (as expressed in *Some Phases of Capital Stock* printed in the May issue) that there is some question as to the propriety of writing off stock discounts. In the circumstances a brief reply is perhaps justified.

Mr. Boyle's first point is that there is no reason why the balance-sheet should show original proprietorship as distinct from accumulated profits since the balance-sheet purports to present the status of the enterprise at a given moment of time and does not attempt to show the history of the business; hence, there is no objection to cancelling stock discounts against undivided profits. This contention is not unreasonable but is perhaps stated a little too roundly by Mr. Boyle. The balance-sheet does not show the history of the business, but probably many accountants would agree that both the past and prospective situations should not be ignored in the preparation of this statement. Surely one reason for the use of valuation accounts to measure the decline in the value of fixed assets, with a consequent retention of cost figures and accumulated expirations for a time at least in the balance-sheet, is the desire to preserve original costs—and not depreciated present values—in the financial statements. Further, some accountants urge that definite contingencies should either be recorded directly in the balance-sheet or in an attached statement. This practice means that the prospective situation is brought into the balance-sheet. Still further, it would surely be admitted by anyone familiar with the taking of inventories and the work of actually preparing the statements that it is only ideally that the balance-sheet shows the momentary condition of a business. It is not considered good accounting, for example, to take into account current prices in valuing merchandise on hand provided the original cost is lower than the current cost.

Referring to an illustration appearing in the article, Mr. Boyle states that "no stockholder has any right to read that the original amount invested was $100,000 or that the total accumulated profits during the company's life are $20,000, but only that these figures represent the present capital and surplus in the business." Assuming this statement to be true it is submitted that what the stockholder has a right to do and what he does do are not the same thing. The typical stockholder undoubtedly attaches the significance of original investment to the par of the stocks outstanding; and he does not understand a technical matter like the cancellation of a discount.

Whether or not it is the function of the balance-sheet to show the amount of original proprietary investment it would perhaps be admitted that this figure is a fact of some importance in any case, and that there is nothing vicious in a proposal to retain this item intact in the statements, if it can be done conveniently.

Mr. Boyle's second point is found in the statement that "if a stockholder wishes to learn what change has taken place in the surplus since the presentation of the last balance-sheet he should refer to the other statements furnished him and in a form that he can readily understand." The writer does not share Mr. Boyle's optimism with respect to the ability of the investor readily to understand the statements usually furnished him; and in any case it should be pointed out that the following statement appears in the writer's article: "It is true that an intelligent examination of income sheet and balance-sheet in conjunction by a person with some knowledge of accounting would serve to explain the disappearance of a stock discount item and a reduction in surplus of a like amount." Since this possibility was admitted in the article why does Mr. Boyle imply that the matter was overlooked?

Mr. Boyle then points out that there are many other ways of subdividing, appropriating, labeling and segregating surplus than its use to eliminate stock discounts. In the next paragraph he criticizes the writer severely for calling attention to the same fact. It should be admitted that in the statement referred to the writer had in mind the abuses which are sometimes practised in regard to surplus as well as the legitimate practices, but Mr. Boyle is quite right in stating that "surely Mr. Paton does not mean to say that the entire profits of a company are to be continually salted down in surplus account year after year and never used for any purpose." In view of this very evident fact, why set up a man of straw and flatten him with such enthusiasm? Further, although it is entirely proper for the directors to make appropriations from surplus, it is to be feared that Mr. Boyle attaches too much importance to the shifting of surplus from account to account (which is often all such appropriations mean.) Such phrases as the "utilization of profits" and the "setting aside of profits" are suggestive of definite action with respect to actual funds of assets and are, perhaps, a little unfortunate when applied to purely formal transpositions of surplus.

In conclusion, the point should be emphasized that the writer's article was intended more as a suggestion than as a statement of fundamental principle. At least it was not even implied that the obliteration of discounts was a peculiarly vicious accounting practice, as it was admitted in several places that the integrity of the total proprietorship figure was undisturbed by such a practice. In view of this fact why so much heat? Why does Mr. Boyle say that in the first paragraph of the article in question, "we are also advised that the accounting profession either does not understand certain matters or in its treatment of them wilfully ignores certain important aspects of them"? What the writer did say was that a study of the texts, articles and discussions of the subject "discloses the fact that either some of these matters are not fully understood or, at least, some of the generally accepted methods of accounting for certain subsidiary phases of capital stock ignore important aspects of the situation." This is an impersonal, carefully qualified, temperate and true statement. Why does Mr. Boyle use the phrase "wilfully ignore", and why does he attempt to construe this modest statement into a deliberate attack upon the accounting profession? This last is the more ridiculous in view of the fact that the texts, articles and discussions referred to are largely supplied by academicians. The writer is frankly at a loss to understand Mr. Boyle's apparent anxiety to misunderstand the tone and content of the article in question.

Yours truly,

W. A. PATON.

Washington, D. C., July 17, 1919.

Oklahoma State Board of Accountancy

The governor of Oklahoma has re-appointed Tom D. Boydston secretary and treasurer of the state board of accountancy for a term of three years. The ex-officio members of the board are S. A. Freeling, attorney general, and Fred Parkinson, state examiner and inspector.

Maryland Association of Certified Public Accountants

At the annual meeting of the Maryland Association of Certified Public Accountants the following officers were elected for the ensuing year:

R. C. Reik, president; C. Wilmer Black, vice-president, and R. C. Morrow, secretary-treasurer.

Herbert J. Brooke & Co. announce that they have admitted George M. Doty to partnership. The name of the firm will be Herbert J. Brooke, Doty & Co., with offices in the Lumber Exchange building, Chicago.

H. W. Courter and Wm. C. Rhyne announce the formation of a partnership under the firm name of Courter & Rhyne with offices at 34 Pine street, New York.

Djorup & McArdle announce that Arthur B. McArdle has been admitted to the firm. The firm name will now be McArdle, Djorup & McArdle.

Scovell, Wellington & Co. announce the removal of their New York office to 27 William street.

Henry Varay announces that he is returning to practice at 20 Broad street, New York.

W. B. Lathrop announces the removal of his office to 327 South La Salle street, Chicago.