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## American Utilities and Asset Values

The Accountant

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# American Utilities and Asset Values

From *The Accountant*

[In THE JOURNAL OF ACCOUNTANCY for January, 1937, there was published the full text of a decision of the United States Supreme Court in the case of *American Telephone and Telegraph Company et al v. United States et al*. In that decision the court denied the telephone company's request that the Federal Communications Commission's order prescribing a uniform system of accounts be set aside. The theory of "original cost," as outlined in the provisions of the prescribed system, had been the subject of considerable controversy. In its issue of May 1, 1937, *The Accountant* (London) commented editorially on the decision of the Supreme Court, and because of the general interest in the subject, the text of this editorial is reprinted as follows. — EDITOR.]

A FEW weeks ago the United States Supreme Court decided an appeal brought by the American Telephone and Telegraph Co. on behalf of thirty-four American telephone companies against a regulation made under statutory powers conferred on the Federal Communications Commission concerning the accounts to be prepared and published by the companies. The matter throws a sidelight so interesting to accountants on the difficulties arising in America out of the policy of tightening up public control of industry that we have reproduced in this week's issue the verbatim report of the judgment of the court. The matter was not localized to New York because a representative of the regulatory commissions of no less than forty-six states was joined as defendant in support of the contested order.

Under the communications act of 1934, it was provided that "the commission may, in its discretion, prescribe the forms of any and all accounts" to be kept by carriers subject to the act, and in pursuance of this duty the Federal Communications Commission prepared a draft of a uniform system of accounts to apply to all telephone companies as from 1st January 1936. Under these regulations telephone plant was to be reflected in the several balance-sheets under four separate headings. In the first three were to be stated the "original cost" of plant, respectively, in service, under construction and held for future use. No point arises in connection with this three-fold separation. The real difficulties centered around the definition of "original cost" which was stated in the regulations to be "the actual money cost of (or the current money value of any consid-

eration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility." If such actual costs were not known in any particular case, then estimates were to be substituted in their place. It is evident that the sum of the quantities included under the first three headings might be either less or greater than the purchasers' investment in the relative property and, in such cases, the difference is, under the regulations, to be taken care of by a fourth account, to be stated separately on the balance-sheet, under the caption "telephone plant acquisition adjustment."

We pause at this point to indicate to the reader that there is some reason behind this apparent midsummer madness of accounting; for, obviously, if once the state begins to undertake the compulsory fixation of rates to be charged to the consumer, the proper figure to be charged to operating costs for the amortization of capital expenditure becomes of prime importance. The difficulty which arose out of the arrangement embodied in the scheme above described might have been foreseen, for the depreciation of the "acquisition adjustment" account leads to a direct conflict of interests between the rate-fixing activities of the state and the income-earning rights of the investor. Accordingly, the official powers over the treatment of the "acquisition adjustment" account became a centre of controversy. On this point it cannot be said that (at any rate as viewed from England) the regulations are clear and unambiguous. The wording used is "the amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this commission may direct." It is not too much to say that the companies seem to have had reason to fear that a regulation so worded might have the effect of removing from them the control of their own financial affairs. It thus seems natural that they should come to the court with the objection that they are prevented from recording their actual investment in their accounts, with the result that the accounts prepared do not fairly exhibit their financial situation either to their shareholders, to external investors or to the taxation authorities.

It is at the point where the court deals with this objection that the English reader finds difficulty in appreciating the terse style

adopted by American judges as contrasted with the more literary eloquence of their English brethren. The American court fell back on the vague principle of "administrative construction." It called upon the commission's chief accountant who testified that the amount carried to suspense "would be disposed of, after the character of the items had been determined, in a manner consistent with the general rules underlying the uniform system of accounts for the distribution of expenditures, according to their character, to operating expenses, income, surplus or remain an investment." We hope we may be pardoned for the comment that this language seems perilously like the gift of a stone in response to a request for bread. Nor was the assistant-attorney-general much more specific when he stated that the commission construed the provision as meaning "that amounts included in the account that are deemed, after a fair consideration of all the circumstances, to represent an investment which the accounting company has made in assets of continuing value will be retained in that account until such assets cease to exist or are retired; and in accordance with the regulations provision will be made for their amortization." The American court did not share our qualms and decided that "we accept this declaration as an administrative construction binding upon the commission in its future dealings with the company." We should have been better pleased had the court obtained a precise definition of "continuing value."

The appellant failed equally decisively on the point that where all record of "original cost" in its defined sense is lost the formulation of an estimate might be nothing better than the merest guesswork; and the publication of a guess in a balance-sheet published as a considered statement of opinion and of fact might lead to results as serious even as criminal liability. The court, perhaps rightly, brushed this aside on the ground that the making of an estimate was specifically authorized by the statute itself.

We realize that we cannot set ourselves up as censors of American conditions, but when we consider that the entire public-utility industry of the United States is likely to be subject to these highly controversial views of accounting we cannot wonder that American accountants are themselves somewhat aghast. The bookkeeping difficulties involved are too obvious to

need explanation and we should have thought that if the authorities desired to place their own interpretation on the highly ambiguous word "value" they might have secured their ends by calling for a re-analysis of balance-sheet figures in the form of a memorandum statement. On the other hand, to impose on companies financed by private capital the obligation to place a connotation on "value" irrespective even of changes in money levels over prolonged periods of time is, from the English viewpoint, highly arbitrary; and we can understand the reluctance of business men, conversant with the details of their own affairs, to submit the financial fortunes of their undertakings to the academic opinion of semi-public officials seated in the inaccessibility of government offices.

The whole matter seems to us to provide a crucial illustration of the dangers of government by administrative order, not without its lessons on this side of the Atlantic, and to prove that capitalism can be killed as easily by the American recipe as by the Russian.