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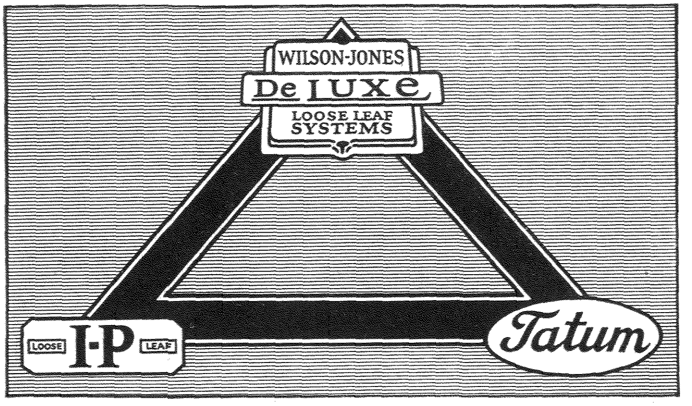

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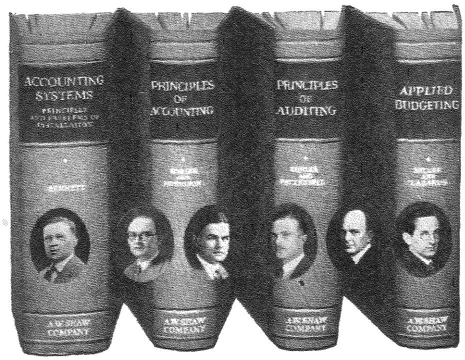

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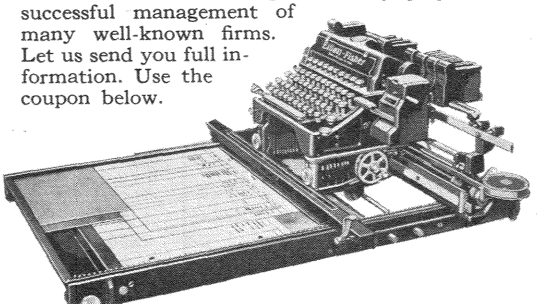

The JOURNAL *of* ACCOUNTANCY

Official Organ of the AMERICAN INSTITUTE OF ACCOUNTANTS

Vol. 48 OCTOBER, 1929 No. 4

American Institute of Accountants

REPORT OF THE PRESIDENT*

By FREDERICK H. HURDMAN

It is both the duty and privilege of your president to report at this time concerning his stewardship during the past year and to present for your consideration such observations as occur to him after that experience.

It seems unnecessary to inflict upon you a résumé of the activities of the year, all of which will be covered in reports of committees and of the secretary. Suffice it to say that the Institute is in a healthy condition with every department functioning, membership increasing and finances sound.

Perhaps the outstanding accomplishment of the past year has been the completion of the revision of the pamphlet "Verification of financial statements," which has been printed by the Federal Reserve Board. The manner in which this revised pamphlet has been received by accounting and banking organizations is indicative of the character of the work done by the committee which labored so long and diligently to make this pamphlet a document of value to the entire accounting profession.

It has been said that no set rules can be laid down for the accountant; that his work is naturally the result of his own brains and that he must be the judge and assume entire responsibility for the extent and thoroughness with which he does his work. Nevertheless, it does seem wise and proper that out of our experience we should set down, in some tangible form, for the guidance of those less experienced, what appears to be good practice and proper procedure.

It is not claimed that this document represents perfection, but it is certain that if all practising accountants would be guided by the suggestions in this pamphlet there would be an immense improvement in the quality of the work done. In most cases the procedure described in the pamphlet will be regarded as a mini-

*Delivered at the annual meeting of the American Institute of Accountants, Washington, D. C., September 17, 1929.

mum and wherever conditions warrant the accountant will do more than is suggested.

This same special committee which prepared the pamphlet "Verification of financial statements" is still engaged, in coöperation with the committee on education, in drafting a classification of accounting services and expects to complete its labor within the next few months. It is interesting to note how the term "balance-sheet audit" has been relegated to the discard. The committee found that while such a term was often applied to an audit there was not entire unanimity of understanding as to what it embraced, and it seemed unwise to have any term generally used which was susceptible of misunderstanding. The committee, therefore, has labored diligently to find terms which would not be misleading and would indicate as clearly as possible the kind of work to be performed.

During the year the president and secretary visited accountants in Boston, Baltimore, Virginia Beach, Indianapolis, Cincinnati, Louisville, Kansas City, St. Louis, Omaha, Minneapolis and St. Paul. In all these places the officers were received with the utmost courtesy and found the accountants, whether they were members of the American Institute or not, interested in what is being done for the profession.

Numerous matters of importance are being considered by the executive and other standing or special committees of the Institute. Your officers have constantly in mind the growing importance of our profession. The American Institute, if it is to measure up to its responsibilities, must keep abreast of changing conditions. With the growing tendency toward mergers in all parts of the country, the accounting profession must, of necessity, adjust itself to meet this economic condition.

A study has been inaugurated looking into the matter of the facility with which accountants may carry on an interstate practice. It is my belief that when regulatory measures are adopted by the states, it should not be made too difficult for an accountant to pass into another state to complete an engagement originating in the state where he maintains his principal office. Investigations of a similar character are being conducted by other organizations and it is hoped that from these studies there will be evolved a plan of procedure which will be of value to all.

The president is deeply appreciative of the work which has been done by members of committees and others who have been called upon to perform service and have functioned in a manner creditable to our profession. It is true, however, that too few of our members are willing to make the sacrifice of time necessary if the Institute is to accomplish adequately all the things it has before it. There should be a greater sense of obligation on the part of a larger number of our members to committee responsibility. The direct benefits to members may not be proportionate to the amount of labor expended, but the satisfaction derived by any member willing to devote the time to working out something which will be of benefit to the entire accounting profession can not be measured. Much time and thought is given to committee appointments and there are few committees which could not perform a useful service if the membership of those committees appreciated the opportunity for service. Too often we are too impressed with our own personal obligations to devote the time required in strengthening the profession generally. It is the sincere hope of your president that a great number of members who heretofore have been inactive will indicate a desire to share some of the responsibilities and burdens which are now being carried by a few members who do appreciate what they owe to their profession. Unless many more of our members who have had large experience are willing to devote time to matters affecting the profession, we can not hope to do all that seems necessary if the Institute is to keep up with the problems which are arising daily and are of vital interest to the profession throughout the country.

Some of you may have read the article, "Honor among lawyers," which appeared in a recent issue of the *Outlook*. This article attempts to analyze the legal profession, and when we find a statement such as

> "We find ourselves today with a profession filled with incompetents, with liars and jury bribers and peddlers of perjured testimony. We find ourselves served by attorneys of no greater cultural attainments than the butcher's boy around the corner and not half his native honesty. We find ourselves responsible to judges who have nothing to recommend them except unsavory political backing and a few years of cheap practice."

it behooves us to stop, look and listen to determine just what progress the accounting profession has made and in what direction it is going.

Some of the reasons given in this article for the condition which is said to exist in the legal profession are:

1. The overcrowding of the bar.
2. The lack of proper educational requirements in the face of the modern complexity of the law.

3. The absence of an efficient disciplinary control.
4. The evolution of the legal profession into a trade.

These are all reasons about which we might very well ask ourselves, do they exist in the accounting profession and, if so, what are we doing to counteract them. We may not have any overcrowding at the present time, but when one considers the rate at which the accounting schools are turning out students, it seems probable that we too, in the not distant future, will have an overcrowded condition. I have been told that there are at present 45,000 students enrolled in accounting schools in this country. Are we, as an organized body of accountants, doing all that we should do to encourage proper educational requirements? Are we too soft in our disciplinary methods? Should we proceed more vigorously in the prosecution of cases which appear to involve a violation of our rules of professional conduct? Is each of us afraid that some day he may make the same error, and are we inclined, therefore, to be tender with the violators of these rules? Are we reaching toward higher and higher standards of professional practice or are we, in the scramble to attain larger and more lucrative practices, veering away from those principles which seem to lie at the foundation of our profession and bending more toward those policies which seem to be peculiarly related to trade?

The president does not wish to appear to be unduly pessimistic but he is fearful that we may settle back into a state of smugness, closing our eyes to the economic changes which are taking place, when we should be ever striving for that state of perfection which we may never hope to attain but can only expect to approximate by untiring efforts and the wholehearted coöperation of the entire membership. The president is convinced that there is much work to be done. He is also convinced that much work will remain to be done, unless there is developed a greater spirit of service on the part of a larger number of members than is apparent at present.

The Institute, through its members, took an active part in the work of preparation for the international congress on accounting, successfully carried to completion in New York last week. Such a meeting and exchange of ideas must be productive of good to the profession.

Sincere appreciation is expressed to all those who have helped carry on during the past year; to the secretary and his staff; to those members who have responded to every demand I have placed upon them. Whatever I may have said to the contrary has been said in the hope of inspiring more members to their responsibility to the profession which they have selected for their own.

The Accountant and the Lawyer in Tax Practice*

By Charles R. Trobridge

There is probably no field of activity other than tax practice in which, generally speaking, both the lawyer and the accountant feel that they are fully competent to act for the best interests of their clients. The lawyer is doubtless of the opinion that he is better fitted than the accountant to handle tax matters, while the opinion of the accountant is that, in most cases, a lawyer should take a back seat, unless and until called upon for advice on questions of law.

The actual condition of affairs is that up to a certain point both are equally capable of handling tax matters, but beyond that point coöperation is not only advisable but necessary.

As I am addressing a body of representative accountants, I propose to devote this paper to the consideration of the conditions under which an accountant should call in a lawyer to coöperate with him in the handling of tax affairs of his clients.

The first question that presents itself is as to why an accountant should consult with a lawyer on any tax problem with which he may be confronted. The answer is that the fundamental training and resultant mental attitude of a lawyer and accountant towards questions of law are, generally speaking, widely different. Taken as a body, we accountants do not possess what might be termed "the legal mind." By training, we are inclined to lean to the equities of a situation. In considering questions of taxation, equity has no place, as tax statutes have to be interpreted according to the strict letter of the law. Most of us have doubtless learned from bitter experience that it is the method by which an end has been achieved which determines whether a taxable profit has been realized, rather than the end which has been achieved. To illustrate: A taxpayer corporation owns securities of which it desires to divest itself. Were it to distribute these securities by way of a dividend, the stockholders would be taxed on the basis of the value of the securities at the time of receipt by them. If, however, the taxpayer corporation sold these securities to a new corporation in exchange for the total capital stock of that corpora-

*Address delivered at the annual meeting of the American Institute of Accountants, Washington, D. C., September 17, 1929.

tion and distributed among its own stockholders said capital stock, no taxable income would be realized by the stockholders of the taxpayer corporation by the receipt thereof.

Perhaps one of the best illustrations of the foregoing is the case of the General Electric Company, which owned securities of considerable value in numerous utilities of which it desired to divest itself. It proceeded to do so by forming a new company, the Electric Bond and Share Securities Corporation, to which it transferred all the securities which it owned in exchange for the capital stock of the new company. The capital stock of this new company was then distributed pro rata among the stockholders of the General Electric Company. The effect of this was to transfer the interest of the General Electric Company in these utility companies to its own stockholders in a manner which resulted in the realization of no taxable income by said stockholders. Had the securities in question been distributed by the General Electric Company direct to its stockholders, then said stockholders would have received income which would have been subject to tax. The attitude of the average man is that differentiations such as indicated above are refinements which should have no place in a scheme of taxation. He, however, overlooks the fact that, as stated above, tax law has to be interpreted according to its strict letter, and not according to equity or common sense. This principle was expressed by an eminent jurist in words somewhat as follows: "Where the law does not specify that the result of a particular transaction should be taxed, then it can not be taxed, however equitable it be that it should be taxed and conversely, where the law specifies that the result of a particular transaction shall be taxed, then it must be taxed, however inequitable it be."

In the course of his training a lawyer studies the interpretation of the law according to its strict letter and also learns in what class of statutes equity can be given consideration. As stated previously, the training of accountants leans rather to equity, but in saying this, I do not mean to infer that no accountants are capable of advising their clients on tax matters, or of suggesting methods whereby certain desired ends may be achieved with a minimum of taxation to those interested. However, I think it will generally be admitted that the greater number of us are so situated that our knowledge of what may be termed the finer problems concerning taxes must of necessity be somewhat meager and no accountant will lose the respect of his client by voluntarily suggesting that in certain questions regarding taxes, the opinion of a lawyer should be sought.

In many instances federal tax problems have to be carried to the United States board of tax appeals, and while a duly enrolled accountant is permitted to practise before that body it is most unwise for him to attempt to appear for his client unless he is thoroughly acquainted not only with the theory but the actual practice of the law of evidence. It is true that in many instances the members of the board before whom the case is presented endeavor to assist the petitioner's counsel to overcome the objections of the representative of the solicitor of internal revenue, but to rely upon such assistance is not fair to the client.

An illustration of what I have previously termed the "legal mind" of a lawyer might be of interest. A lawyer propounded to me the theory that the portion of the depreciation reserve which represented accrued depreciation on assets which had been paid in for stock should be included in invested capital. The grounds on which he based his theory were that invested capital was a statutory concept and that inasmuch as the law stated that invested capital meant actual cash value of tangible property, other than cash, bona fide paid in for stock or shares, at the time of such payment, the taxpayer was entitled to have such value included in computing his invested capital, and that to rule that in determining earned surplus provision must be made for depreciation on such tangible property was in effect to deny to the taxpayer his legal right to include in invested capital the full value of the property paid in for capital stock. Unfortunately, neither he nor any other lawyer, so far as I am aware, has carried the issue beyond the income-tax unit, but, it does not therefore follow that there is no merit in the theory.

I think it will be admitted by most accountants that they would never have propounded such a theory, because their training was such that under no stretch of imagination could they regard depreciation reserve as earned or any other class of surplus, nor could they consider that earned surplus could be determined without making due provision for depreciation.

While problems affecting invested capital are of little interest to present-day practitioners, there are still many problems in which a lawyer's viewpoint would be of great assistance to accountants, because in preparing or reviewing tax returns, or combating proposed additional assessments, all angles of the case must be considered, in order that every possible claim may be made on behalf of the client.

It is axiomatic in tax practice that, generally speaking, one receives no more than one asks for, as, however good may be the intentions of the treasury department it has to be admitted that as a matter of practical politics that department has not the force nor the time to give to making extensive searches for possible grounds of refunds to taxpayers. On the contrary, its main efforts must of necessity be directed toward the collection of additional assessments. This being the case, a taxpayer in order to protect himself has only two alternatives, viz.:

(1) To prepare his return on the basis most favorable to himself, in which he takes advantage of every possible deduction to which he feels that he is legally entitled, whether in accordance with treasury-department rulings or not, and

(2) To prepare and file a return on the basis which is strictly in accordance with the department rulings and to file a claim for refund of overpaid taxes, based upon the additional deductions which are not admitted by treasury-department rulings, but to which he believes he is legally entitled.

Most taxpayers decide to file a return which indicates the lowest amount of taxes payable and to hope for the best. This being so, it is therefore beyond question that where an exceptional case arises, the accountant would be well advised to talk it over with an attorney. The question of whether the matter should be taken up with an attorney who is a specialist in tax matters or with one who is a general practitioner is open for discussion.

The tax specialist can, in most cases, best interpret the treasury department's probable attitude on the question at issue and because of his frequent contacts with that department can advise as to the best method of procedure. In most cases he will have an office, or at any rate a correspondent, in Washington, which is a distinct advantage, as it is beyond question that constant, personal contacts with the representatives of the department are of great help not only in presenting cases at conferences, but also in following them up.

On the other hand, while a general practitioner will not be so familiar with the treasury department's procedure and practice, he will come to the problem with an open mind, with the result that he may develop methods of approach to it which may not suggest themselves to a tax practitioner whose mind is steeped in treasury-department rules and regulations and in decisions of the courts and United States board of tax appeals.

Tax problems which confront accountants arise in connection with both federal and state taxes, but principally the former. Some questions may arise in connection with local taxation, but they are relatively few and for that reason are not discussed herein.

Due to varying conditions existing in the forty-eight states of the union, I hesitate to express any general opinion as to whether an accountant or a lawyer is the better able to handle state tax problems. In some cases it is undoubtedly to the advantage of a client to have state tax matters handled by a lawyer familiar not only with the law but with peculiar local conditions. In others, and particularly where the basis of taxation is the income as reported for federal tax purposes, an accountant should be as fully capable of handling tax problems as a local lawyer. Even in such cases, however, there are times and occasions when a "well acquainted" lawyer would be a valuable adjunct to an accountant.

There are a few states, such as Massachusetts, which have evolved a form of return the preparation of which is reputed to have driven more accountants insane than any other cause. The return is something like a cross-word puzzle; if one is able to fill in an amount in each blank space, it is solved. If there are any blank spaces unfilled, then there is something wrong. I have heard it rumored that the basis of assessment in Massachusetts is so elastic that if one was advised by the tax commissioner of Massachusetts of the formulæ which he used in determining the tax for a particular year and the return for a succeeding year was filed on the same basis, the assessment that would be made by the tax commissioner could not be checked by the application of the formulæ used by the tax commissioner for the preceding year. This being the case, it is evident that the lawyers of the state of Massachusetts put one over on the accountants.

The majority of the problems of taxation with which accountants are confronted relate to federal taxes. It is therefore to these that I propose to devote my concluding remarks:

The federal tax practice of an accountant may be divided into three fields, viz.:

(1) The preparation of returns.

(2) The reviewing of returns and also of revenue agents' reports.

(3) The preparation of petitions and the handling of cases before the United States board of tax appeals.

The work of preparing returns is usually more or less routine and the assistance of a lawyer therein is not necessary. There are cases where exceptional conditions have arisen, or where an accountant is called in for the first time to prepare a return, where the advice of a lawyer on certain problems is desirable. In reviewing returns and revenue agents' reports, questions may also arise in which the coöperation of a lawyer would be advisable. In the majority of cases, however, an accountant familiar with the handling of tax matters should be able to carry the matter through the office of the local revenue agent in charge and through the income-tax unit in Washington.

If the amounts in dispute are large and a conflict develops between the accountant and the representatives of the commissioner of internal revenue on either facts or questions of law which appear incapable of a satisfactory settlement, it will then be advisable to arrange for an adjournment of the hearing with a view to presenting further evidence and submitting briefs in support of the taxpayer's case. In the majority of these cases, the assistance of a lawyer in the preparation of the evidence and briefs should be obtained, because the case is arriving at that stage where the next step will be the issuance of what is known as a "sixty-day letter," advising the taxpayer of the final conclusions of the commissioner and of his right to appeal to the United States board of tax appeals. When this stage has been reached, for reasons stated previously herein, the services of a lawyer are, in practically all cases, necessary, and it is therefore only fair, both to the lawyer and to the taxpayer, to associate the lawyer with the case in its last stages in the income-tax unit.

Organizing and Conducting an Accounting Practice*

By George S. Olive

Please consider that this paper which I am presenting today is a report on a special examination which the officers of the American Institute of Accountants have asked me to make as to conditions and tendencies in public accounting practice, particularly as relating to practices which are local to a community, with reference to the extent of the service rendered, and correspondingly small in size. As my examination has been necessarily limited by my own experience, having been entirely in a rather self-contained business community of medium size, my observations may fall considerably short of fitting conditions in a practice of comparable size in the larger cities.

My analysis of the character of such practices at the end of the period under review compared with the same factors at various dates over the past ten years discloses that while the work ten years ago was almost exclusively detailed work on audits of the accounts of business concerns, with the preparation of reports evidencing the work done, marked changes have occurred during the period in the kind of services performed and in the position of the public accountant in the community. These changes are due to many causes, the most important of which are noted below:

First, due to the financial requirements of the world war, federal income taxes became during 1917 and subsequent years the most important single disbursement by most businesses, and the need for an accurate determination of the amount of taxable income and invested capital made necessary a great deal of constructive work on the part of the public accountant.

Second, the owners and managers of businesses have come to realize more clearly the value for credit purposes of reports from independent accountants.

Third, there has been a marked tendency toward the nationalization of business, with a resulting number of sales, mergers and consolidations of smaller units into larger ones, with a greater degree of ownership by the public. Every case of this kind has

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emphasized the fact that the public accountant is indispensable in such transactions.

As a result of these developments, the demands of the business public for our services have undoubtedly increased during the decade at a rate faster than corresponding requirements for any other class of professional work. While a few years ago, practically all of our time was devoted to auditing and the preparation of audit reports, it is now taken up to a considerable extent with consultations with clients, their attorneys and their bankers with reference to the past history or to the future prospects of the business. Formerly it was too frequently the case that business executives took some action and discovered months or years afterward that they might have avoided complications in income tax or other matters if they had followed some well considered plan, developed by their attorneys and their accountants.

These changes in business conditions have resulted not only in making necessary a higher caliber of accountants and other assistants in the organization, but have even affected the character of the office layout and equipment. Whereas formerly even the partners in a small firm, or the head of the organization, were away from their own offices a considerable part of the time, working at the client's place of business, and a so-called "staff room" crowded with small desks was sufficient for the needs of the other accountants, the principal's time is now devoted almost entirely to work in his office, in consultation, supervision and direction. The staff accountants also, under the plan of organization which will be suggested, respond with better work when they are provided with offices in which they can prepare with more privacy the reports which are to reflect the results of their examinations.

I have intimated heretofore that much of this new work which has developed for us is of a kind which attorneys and accountants coöperate in handling. I have found that the leading firms of attorneys are quite willing and anxious to work with us on such matters and that in spite of the regrettable lack of training in accounting theory and practice in the customary legal education they do recognize the necessity of their clients having their transactions conform to good accounting practice. Prosecution of cases before the treasury department and the United States board of tax appeals has developed the interdependence of the two professions and the overlapping of legal and accounting practice is becoming more evident every day.

As to the physical plan of a public accountant's office and its equipment, the furnishing and the furniture must be left to individual tastes, as we probably should have as much difficulty coming to an agreement as we apparently have in adopting a definition of earned surplus. An attractive and well furnished office will impress your clients, both real and prospective, with evidence of your success. I hope that I can, however, impress you with the reasonableness of my unorthodox ideas with reference to doing away with a staff room. Any man who has the capacity and ambition to get started in public accounting, and for whose services charges are to be made on the basis that he is an experienced and capable accountant, is deserving of a quiet, well lighted and well furnished room as his business home. He can not do work of the kind which should come from our offices, using a small space in a large room with a number of other accountants. I believe that it is advisable to provide in accounting practices of medium size either a single room for each man or one room for each two men who are permanently on the staff. This will help to bring out the best qualities of the individual assistants.

This brings me to further consideration of the accountants who are taken into any practice either as employees or as junior partners. The judgment exercised and good fortune of the principal in selecting associates is the one point more than any other that determines whether the accounting practice will grow and obtain and extend a good reputation. To these associates, regardless of the extent of our supervision of their work, do we entrust the reputations which have cost time, money and hard work to build up. It seems quite unnecessary to emphasize the desirability of choosing these men from those who have been well prepared by adequate school and college training, men of integrity and personality who appear to have some natural liking or aptitude for the work. Such men will take as much interest in preserving and extending the standing of the organization as the principals themselves. Proper leadership of the principal will of course inspire the assistants to follow his example and even to compete with him in the service rendered to clients, the final outcome of such a situation being that the employee feels that he is working with the principal and not for him.

The antithesis of such a careful selection of assistants is unfortunately prevalent among some of the larger firms in the larger cities. It seems quite unreasonable to expect to obtain capable men for professional accounting work on a temporary basis at the end of the year for a three-months' engagement; if they were really the kind of men we needed, we should probably be unable to hire them in these circumstances. We should certainly criticize severely any business or industry which tried to obtain the services of experienced and well educated men in such a way. I do not believe that this custom prevails in the case of smaller practices, as it is generally possible by careful planning to offset to a considerable extent the seasonal character of our work, and the severity of the end-of-the-year load of work is not so noticeable.

There are two principal ways in which the smaller firms can offset the use by most businesses of the calendar year for their accounting periods. One is by getting some of the clients to use some other period for closing their accounts when the character of their business is such that the annual closing of the accounts can conveniently be made at the end of some month other than December—to use the "natural business year" of that industry. The other way the small practitioner may relieve this condition is by arranging with clients so that work may be done on the current audits at various times through the year; after the accounts are closed the final audit work can then be completed with little delay, and the plan works to the mutual advantage of client and accountant. Another factor beyond our control, which, however, has been helpful in spreading out the work over the year, is, with accountants who take care of the tax matters of their clients, that the federal and local taxing authorities do not have any favorite time for attack; they are likely at any time of the year to require reports or to make some claim which must at least be investigated and possibly defended. I believe that it will be found possible, if plans are carefully worked to that end, to minimize the bad effects of these peaks and valleys of our work, so that a staff of permanent employees may be kept reasonably busy throughout the year. This planning is, of course, one of the important duties of the individual in the firm who distributes the work, thus preventing delays and rendering the services that attract the goodwill of the clients.

If we regard as our principal function serving the business public in connection with the increasing complexities of its affairs, we must be prepared to render this service at whatever time conditions demand it. Whether or not we are in this desirable situation depends entirely on the ability we may have exhibited in organizing and equipping our establishments. First and most important, do we have associated with us accountants of experience and capacity, and have we exhibited confidence in their ability to the extent of placing on them all the responsibility they were willing to assume, so that they have grown with us to the point where they can help us establish and maintain that most valuable asset of any professional organization, a reputation for integrity and good work? In my opinion such a group can best be brought together from men, who, having had the advantage of a good education and preferably a college degree, have spent several years in handling the accounts of various kinds of businesses. Such men will have had practical experience which enables them to work into public accounting much more quickly than the beginner who hardly knows a charge from a credit. Again my ideas are unorthodox, because the conclusion has forced itself on me that it is neither necessary nor desirable to use men in a medium-sized accounting practice who are commonly known as "juniors." If you object that there is always a great deal of "pick-and-shovel" work on most accounting engagements, I must answer that such detailed work can be reduced materially in volume by the exercise of good judgment and knowledge gained from accounting experience; the total cost to clients on accounting engagements where "senior" accountants only have been used is generally no more and frequently less than where a great deal of the work has been done by "juniors." The quality of the work produced is always better because all parts of the engagement have been handled by accountants who were able to discharge their responsibility satisfactorily. One of these men is in general charge and conducts the work through to the preparation of the report, with more or less frequent conferences with the principals. When the report is completed, it is submitted with the working papers for approval of a partner or other principal, whose examination of the papers is supplemented by discussion of the report with the accountant in charge. There is nothing new about this procedure; I am writing it down, however, because too frequently do we learn, through claims made against public accountants or through trials of members by organizations, that these steps of prime importance are frequently overlooked. Accounting firms, large and small, have in some cases spread themselves out to the extent that work has not been properly supervised. Such regrettable occurrences bring out one of the forceful arguments for having only experienced men as assistants.

Accounting offices of the size now under consideration do not often have occasion to work on engagements requiring the services of very many men; most of the work will be cared for by from two to four men, and with these men working separately on the different elements of the accounting records they gain a breadth of experience which enables them to handle almost any kind of a situation, subject, of course, to consultation with the principal on any matters which are unusual or on which there may be divergence of opinion among those working on the engagement. While the work is extremely varied, the accountants associated with such an office have opportunities to specialize along one line; they are general practitioners just as surely as was the old family physician, and they obtain a wide experience in examining and interpreting the accounting records of almost every type of mercantile and manufacturing business, public utilities, financial organizations and that growing group of organizations which are formed not for profit but to care for the charities and the educational and social needs of the community. In spite of the general character of the practice, however, some of the men will of necessity become more experienced and capable in handling some one or more lines of business activity.

I remarked heretofore in this paper that the position of the principal in an accounting organization in his relation to his clients and prospective clients is materially different now from what it was ten years ago. This is so not only because he has been recognized as an important factor in the proper conduct of business affairs, but also because he has in most cases been quite ready to admit his obligation to the business community by serving it in whatever way his ability and inclination directed him. He owes to the community which has given him material success a debt which must be repaid, and evidence is at hand that public accountants are doing their share in the public work which must be done in every city. Such public service, of course, will not only make necessary the contribution of a considerable part of the time of the principals but also will call for a considerable amount of work by the organization on a basis which will little more than cover cost. Please do not think I impugn the motives of these public servants when I point out that there are some compensating advantages in the form of public mention in connection with this work. As Mr. Ruckstell stated last year in his admirable report to the Institute as president, "Certain professions, like certain kinds of business, do not openly or directly advertise, but publicity helps them. . . . Those who did no advertising, but got public mention when the quality of their work was favorably commented on by printed page or oral dissemination, would be sought out and patronized by the class of clients that could afford to pay."

Assuming that this accounting practice is now well organized with an adequate number of well educated, experienced accountants, all of the status commonly referred to as "senior," and that the business home of the organization is well planned to make it a desirable place to work, what of the other factors which will determine the degree of success of the accounting practice? Among these are the proper use and control of working papers, the development and maintenance of good office records and files, and the coöperation of the office assistants who help us to prepare the reports of our examinations in a form creditable to the organization. On the matter of working papers, the profession now has the advantage of two books, one by J. Hugh Jackson and the other by Messrs. Palmer and Bell, which cover the subject so well that I should waste your time discussing any particular feature. With all the accounting literature produced during recent years, however, I recall only one book (Kester, vol. III, pp. 423–463) dealing extensively with statistical or accounting records of a public accounting practice. This might lead us to assume that we are expected to know our own business, that we are not quite so neglectful of our affairs as the proverbial blacksmith was of his horse. I do believe that any successful practice has of necessity provided itself with adequate records and that a description of the system with which I am most familiar would not serve any useful purpose. On the matter of office personnel, a public accountant should be interested first of all in making sure that his clients' interests are adequately served; one of the principal factors in this connection is a permanent staff of report writers, typists and proofreaders who have the ability to produce from the original rough copy of the report, which is sometimes all too original and rough, a finished document that brings our work most favorably to the attention of our client. Again it takes time and judgment and good fortune to build up such a group of workers.

In conclusion, I believe that notwithstanding loss of clients by the small accounting practice which is apparently certain to occur through mergers, consolidations and other evidences of the nationalization of business, there is still an expanding field in the profession for the small practitioner. He can and should make for himself a position in the community that is peculiarly his own; in his contacts he can make himself favorably known not only where the results of his work are to be used, but by showing his ability and experience through writing in trade publications and speaking to trade organizations and maintaining active membership and interest in the professional societies which are working for the good of the accountant and the profession.

The Development and Effect of Chain Stores*

By Albert H. Morrill

Some one has said that the object of government is the greatest good to the greatest number. Actually government is nothing more than a composite expression of the consensus of opinion generally as to what is best for the economic and spiritual welfare of the people as a whole. It follows that what is best for the majority of the people constitutes the greatest good to the greatest number in their daily economic life as well as in their governmental existence.

While talking to you today I want to look at the economic aspect of the chain store, not as a partisan, which frankly I am, but from the broader viewpoint of one interested in what will do the greatest good to the greatest number; not from the narrow and material viewpoint of how chains may prosper and expand, but from the viewpoint of what, through the years and the centuries, will be the most benefit to the great mass of our fellow countrymen and will promote the life, liberty and happiness of these beloved United States.

If chain stores are economically unsound, if they tend to and ultimately will, through concentration of power in the hands of the few, produce inevitable abuse, stifle initiative and throttle competition, then they should be regulated and their activities curbed. Under our system of judicial interpretation of legislative acts and constitutional provisions, a way will be found to accomplish this very thing, if it is advisable. If chains do not render the greatest good to the greatest number they should be discouraged and the hounding of the chains, a favorite occupation with some at the moment, should be continued.

But if on the other hand—and this years of experience teach me is the case—chains stimulate competition, increase initiative, avoid abuses, raise the standard of business ethics and above all give to the consuming public better goods at lower prices, then no individual or class of individuals, no matter how their personal interests may be hurt, have the right to harass, criticize or attempt to destroy such an agency for good.

*Address delivered at the annual meeting of the American Institute of Accountants, Washington, D C., September 18, 1929.

If chains do render service that is the greatest good to the greatest number they should be encouraged and protected.

Without more to-do let me plunge into the history and present conditions of chain stores.

About one hundred and fifty years ago a marked and unusual development took place in industry. It resulted from the introduction of steam and machinery into the field of production. Once started, its irresistible momentum carried methods of production to their present marvelous achievements.

One of the distinguishing features of that movement is specialization, often referred to as division of labor. But the movement went vastly farther than the term specialization would indicate, for it has come to involve not only the division of the parts of a process among different men in a plant but their distribution among different plants often located in widely separated places.

But production, however efficient, scientific and standardized, is useless without distribution. The commodities produced must be distributed to the consumer. Methods of distribution have not kept pace with methods of production. They have lagged far behind production methods in the race to produce efficiently and scientifically, and thus give the greatest good to the greatest number. In the efforts of distribution methods to keep pace with production methods, complications have arisen which until comparatively recently have received wholly inadequate attention. No matter how efficiently and economically a machine, a garment or a food product was produced it reached the consumer, for whom it was created, only after passing through a long, cumbersome, inefficient and expensive passageway.

In valuing our modern economic system it has been a commonplace thing to point out the need of some means for reducing the expenses of placing commodities in the hands of the consumer.

While professors of economics, political orators, congressmen and even presidents have railed against the cost of distribution, without furnishing a solution, it has remained for the chain store to provide the most promising agency for solving the difficult problem.

Once fairly started, the chain-store idea has grown by leaps and bounds until it is today recognized, by all conversant with the modern system of marketing, as the outstanding contemporary development in the field of retail distribution.

The chain, a comparatively recent claimant for public approval, has of necessity clashed with many established traditional methods. Keen opposition to the chain has been voiced by those who are still using these traditional methods. Through this opposition the issue has been clearly joined between chain stores and those whose interests are or are thought to be threatened by the success of the chain system.

In passing, it is interesting to glance back through the pages of history and to see whether past innovations and departures from traditional methods have met opposition similar to that presented to the chain. There are many such, but I shall content myself with referring to only a few.

In the latter part of the eighteenth and early part of the nineteenth centuries throughout all England there were pamphlets distributed, editorials written, fiery speeches made, legislation threatened and actually introduced in parliament and violent attacks made by mobs in some instances, all because of the charge that the weavers of England were about to be driven out of employment and into the poorhouse because of the introduction of the looms and other machinery in the weaving trade. The looms were established, the agitation subsided and in less than a generation it was seen that far from injuring the craft of the weavers it had shortened their hours, increased their wages and given to the great mass of the people better cloth at lower prices.

As late as the middle of the last century there creaked and groaned, slowly and laboriously over the atrocious roads between Albany and Buffalo, New York, long lines of animal-drawn, heavy-laden wagons transporting goods from the Hudson river to the Great Lakes. Thousands of men, thousands of horses and thousands of dollars were employed in and around this picturesque and rugged industry. A group of New York and Boston capitalists, visualizing the possibilities of the only recent application of steam to rail transportation, applied to the New York legislature for authority to incorporate and construct a railroad between Albany and Buffalo. Immediately a hue and cry arose. Impassioned memorials in opposition to the project were addressed to the legislature. Associations of merchants along the wagon routes protested against granting these capitalists the right to ruin their business. Innkeepers, horse breeders, wagon builders, teamsters all joined in a protest against this new method of transportation as destructive of traditional methods which would deprive them of their property and livelihood. It is unnecessary to recite the stages by which steam-railroad transportation supplanted animal-drawn vehicles and the great benefit and development that resulted to the people as a whole.

These two illustrations, to which might be added a dozen others, show that history is merely repeating itself in the present agitation against chains. The opposition comes not from the people as a whole, but from that small minority accustomed to the use of traditional methods who find themselves in the path of progress as represented by chain methods of distribution which give to the consumer at least as good if not better products at a lower price. The opposition comes not from the people as a whole because they, by their ever increasing patronage of chain stores, register from month to month and from year to year their approval of this means of distribution. It comes solely from the counterpart in our present day of the weavers, teamsters and innkeepers of a century or more ago. As the former opposers of modern methods were benefited rather than harmed by the use of the new methods, so the present-day opponents, ten years hence, will find that they have been benefited by the chain methods.

The benefits of chains are too numerous to be recited in my limited allotment of time. It has been said and well said that every commercial venture "will flourish or decline in proportion as it serves or fails to serve the public needs more efficiently and economically than competing agencies."

This is the test that should be applied in judging the chains, and according to whether they do or do not improve the service of distribution to the public they should be approved or condemned.

Chains are not public utilities operating under a special privilege granted by the states. They can be crushed within the year by the withdrawal of public patronage. They succeed not because of patent rights or special formulas but because the public approves of them. As long as chains continue to give better goods at cheaper prices they will continue to grow and their growth will be due solely to public favor. Can there be a simpler or more conclusive expression of public favor than the continued increase in patronage of the chains? Do we need a nation-wide referendum for or against the chains? Such a referendum is taking place every buying day of every year and the people are registering their approval by the thousands who increasingly patronize the chains.

The reason for the public's approval of chains is perfectly apparent. Statistics covering the industry as a whole are not strictly accurate, but such as they are they conclusively show the reasons why chains succeed under continued and increasing public patronage. They succeed mainly because of the quality of service rendered. Their main service is to furnish the same product at a decreased cost to the consumer.

It is impossible to determine accurately the amount of this decreased cost, but a few figures are illuminating. In 1927 the total estimated grocery sales in the United States amounted to $7,500,000,000. Of this amount, it is estimated, the independent or unit system of stores contributed $5,000,000,000 and the chain systems $2,500,000,000. Based on the known savings which the chains make for the consumer as compared to the unit system of stores, during that one year, there was saved to the consumer in the United States by the chain grocery systems $300,000,000. If the chain systems had distributed all the groceries during 1927 there would have been a total saving of $900,000,000 to the consumer.

These figures are not accurate. But they are fully substantiated by accurate figures taken from the report of the company with which I am associated, the Kroger Grocery & Baking Co., and for these figures and the deductions drawn from them I am indebted to the publisher of the *Chain-store Age*.

During 1928 the public paid Kroger $207,372,551. The products thus sold cost Kroger $173,737,555. Had the public purchased the same products through regular wholesale and retail channels it would have paid $243,510,000, just $36,137,450 more than it actually paid.

In arriving at these figures I am taking the average operating costs of wholesale and retail grocers established by the Harvard bureau of business research. That bureau says the average wholesaler's and retail grocer's gross margin aggregates 30.4 per cent. of his sales. Applying this operating ratio to Kroger's gross sales we see that this company alone saved the consumer more than $36,000,000 in one year.

Continuing, Kroger's operating statement for 1928 shows that operating expenses and depreciation plus profit equaled 16.2 per cent. of its sales, of which 2.3 per cent. was operating profit plus .62 per cent. of other profit, making a total net profit of 2.92 per cent. on sales. The consumer obtained his products from Kroger with one mark-up of 16.2 per cent. and from the independent or unit store with two mark-ups aggregating 30.4 per cent.—almost double that of Kroger.

These figures completely substantiated those given earlier, which estimated a saving to the consumer in the United States of $300,000,000 annually through chain distribution and a possible saving of $900,000,000 annually through distribution of all food products by chain-store methods.

When I suggest the distribution of all food products by chain methods I do not even intimate that all food products should be distributed by one or a dozen or any number of large chains. What I mean is that chain methods of distribution should be used by large chains, by small chains and by the unit stores, whether operating individually or through association with other unit stores now commonly known as voluntary chains.

Reverting again to the work of the Harvard bureau of business research, this bureau states that the consumer, in purchasing from a chain, saves 11.3 per cent. on the price he would pay the independent. It states that the operating expenses of the chain average 15 per cent. of its sales and of the unit store 17.3 per cent. of its sales. Again it states that the chain store averages 27 per cent. net profit as against the average of unit stores of 1.8 per cent. net profit. From this the bureau reaches the conclusion that the consumer, when he buys from the chain, gets as much for 87 cents as he would get for $1.00 from the unit store.

It needs no extended argument to show why the public patronizes the chain.

The chain's success depends not on special privilege for its field, and opportunities are open to everyone. It depends not on questionable practices, for questionable practices can be pursued with comparative immunity by the small, obscure distributor. They may not be pursued with impunity by the large chain which is subject to the light of publicity, the attack of its opponents and the searching investigation of governmental commissions. The success of the chain, analyzed, is due chiefly to personnel, purchasing power and advertising. It brings to every "string town on the pike" a wide choice of standard commodities; it sets standards for products, service, courtesy, window display and cleanliness that not only operate to the advantage of the consumer but stimulate and awaken new standards, ideals and activities in the mind of the unit-store owner. It brings to the smaller community higher types of personnel and methods. It gives to the butcher boy, the grocery clerk, the store operator in its employ, unlimited opportunities for advancement, for as far as we know there is not an operating head of any great chain today who a quarter of a century ago was not occupying a humble position.

Far from taking money out of the community, as is often charged, the chain keeps money in the community. It pays the same rent, the same taxes, the same charge for hauling and freight transportation as is paid by others, but more than this it saves to the consumer in a community vast sums which are retained by the consumer and spent in that community for other purposes. To be specific, in the communities served by Kroger there was saved to the consumer more than $36,000,000. This sum did not go out of the community. It remained in the pockets of the consumers to be dealt with as each consumer saw fit.

We do not wish to be ungenerous to our competitor, the unit storekeeper. He serves large numbers in the community and if his methods are modern he not only survives but prospers. We do not criticize him on our own initiative when we refer to the findings of the United States bureau of the census based, by it, on the Louisville grocery survey made at the request of the Louisville Retail Grocers Association. The bureau of census, impartial and desiring to be helpful, was forced to a stinging criticism of the methods used by unit stores. It says, in part, "one store inventory was nothing less than a grocery museum." It carried a conglomerate mass of obsolete groceries, notions, dry-goods, drugs and hardware items. Some of its food products were three years old. It made no effort to move its dead lines or to attract customers by selling standard goods at lower cost to the consumer.

In another instance the survey found that of two stores in the same neighborhood, both in competition with the chains, one did a gross annual business of $115,000 on an inventory investment of $3,000 and the other did a gross annual business of $25,000 on an inventory investment of $3,500. In one case the ratio of volume to inventory was 37 to 1, in the other it was 7 to 1. In one case the institution was profitable, in the other it was not.

The preliminary report on this survey contains not one finding that the difficulties of the unit store are in any way concerned with the competition of the chain. It does find that "Louisville retailers are self-indicted; they are proven guilty. But nothing revealed here is peculiar to Louisville. All through the country, grocers are following the same methods for want of precise knowledge of what they are doing and what it is doing to them. The Louisville wholesalers are convicted as accessories, if not abettors. The manufacturers who sell direct are convicted of inciting the aggravating and prevailing practice. And the consumer pays the bill—a heavier bill than is yet apparent."

So it appears from this and many other authorities that the chain is not the cause of the difficulties in which the unit distributor finds himself. His difficulties are due to an inertia which causes him to cling to and be contented with traditional obsolete methods. If he continues to cling to them he will be trampled upon by the irresistible march of modern methods. Such has been the history of the world and no amount of legislation or abuse can prevent it. But he can survive and prosper. Many of his kind have done so and are still doing it.

Some years ago a merchant in a western city found himself owner of the building in which Penney Company operated and at the same time in competition with the Penney Company. At the expiration of Penney's lease it was supposed that the owner would oust his competitor, Penney, from the nearby premises. But the owner did no such thing. He renewed the lease with the statement that Penney's methods, prices and general atmosphere not only had taught him many things about his business which he did not know, but had also actually increased his business. He desired Penney to continue as a competitor in as close proximity to his store as was possible. Just another illustration of the fact that the chain, far from crushing competition, increases it and benefits not only the public at large but the wide-awake, aggressive and enlightened unit storekeeper.

I shall not refer, except in passing, to the methods used by the opponents of chains in endeavoring to create public sentiment hostile to the chains and, by this public sentiment, to tax chains out of existence. The methods in many instances are supported by positive misstatements, always the resort of him who does not have his battle just. In every instance the methods are economically unsound, unjust, discriminatory and have for their purpose the benefiting of a few at the expense of the many. Every burden by way of tax or otherwise placed upon the chain is in reality placed upon the consumer. Suffice it to say that in every instance in which this regulatory and destructive legislation has been presented to a court of final jurisdiction, and in most instances when it has been presented to the legal advisors of the state, they have had courage and the character to declare it unconstitutional.

No one of the great chains has sprung full grown from the brain of a man, as Minerva did from the brain of Jupiter. Every great chain has had its beginnings in one small store. The determination, the industry, the vision or service of one man or group of men gave to the people the service they wanted. No unit store today but would like to become a chain. No producer or wholesaler but craves the patronage of a chain.

To repeat, the real answer to the question under discussion is service. The outstanding service which the chain renders to the nation is increased standard of products at decreased cost to the consumers.

Americans are the greatest developers of efficiency the world has ever known. The efficiency and economy of chain distribution and the inefficiency and costliness of unit distribution is conceded by all. The efficiency of this nation added to unlimited energy, fertile, investitive and great national resources have made our standard of living the highest ever known to the world. By this combination of qualities we have produced the greatest good to the greatest number. We will continue to demand the same standard during the centuries, through which this nation will survive and prosper.

But greater than the nation, greater even than the constitution, are the people of these United States from whom flow all power. Eventually they will crush an economic wrong as they did slavery. Eventually they will support and demand an economic policy that is right. Eventually they will adopt that policy which furnishes the greatest good to the greatest number. They will approve and insist on the economic service of better goods at lower prices brought to them by the chains. They are now approving and have approved this service by their daily and ever increasing patronage of the chains.

Accounts of an Importing and Exporting House

By Glenn L. Brown

Owing to the enormous increase in the number of concerns in the United States that are now doing more or less of an importing or exporting business, the practising accountant is coming in contact with the problems of this kind of accounting more frequently than in the past and undoubtedly will be called upon still more often in the future by his clients for advice as to the methods of handling this class of accounts. In recording the transactions of a company engaging in this business, problems are continually arising that are not met with in the accounts of a concern that limits its activities to a strictly domestic business.

It is not the purpose of this article to attempt to outline a cut-and-dried system of accounts that will meet all the requirements of any exporting or importing house, as no system is absolutely perfect. The needs of each particular business must be studied before an entirely satisfactory system can be installed. I confine myself, therefore, to a general outline of the methods used in handling a few of the problems encountered in the accounts of a particular concern whose stock in trade is obtained in the following manner:

1. Merchandise purchased by the company's travelers in foreign countries
2. Merchandise shipped direct to the company by foreign dealers
3. Merchandise purchased in the United States
4. Merchandise manufactured by the company

The company handles four distinct classes of merchandise and the accounts are so arranged that a gross trading profit can be readily ascertained on each class of domestic sales and each class of foreign sales.

Before the goods are sold they are held in stock, in storage and on consignment.

This company has at all times several travelers in foreign countries purchasing merchandise. When a traveler starts on his trip, which usually lasts a year or two, he is furnished with two letters of credit—one for the payment of his expenses and the other to be used in payment for merchandise purchases. For the recording of these letters of credit, the company has two control accounts in its general ledger. They are brought into account by journal entry as follows:

Letters of credit—issued to travelers.......	Dr.	
To Letters of credit—issued by banks ..		Cr.

A detailed memorandum account is kept recording the transactions on each letter of credit so that the status of each credit can be ascertained at any time.

An expense account is kept for each trip and as drafts on letters of credit for expenses are presented, they are paid by cheque and the respective expense accounts are debited.

The drafts in payment for the purchases of merchandise are generally 90 or 120 days' sight and, upon presentation and acceptance of them, the following entry is made upon the books of the company:

Importation advances....................	Dr.	
To Unpaid-drafts account.............		Cr.

When these drafts are taken up, the entry made is as follows:

Unpaid-drafts account	Dr.	
Interest and bank commission on drafts....	Dr.	
To Bank account....................		Cr.

At the end of each month a journal entry is made—

Letters of credit—issued by banks.........	Dr.	
To Letters of credit—issued to travelers		Cr.

for the aggregate amount of drafts on letters of credit presented during the month.

In the case of direct shipments of merchandise from foreign dealers, the general practice is for the shipper to draw a draft at 90 or 120 days' sight for a previously agreed percentage of the value of the merchandise. The drafts are often drawn in sterling or some other foreign exchange. The manner of booking these drafts is similar to that used in the case of drafts drawn by the company's travelers, except that before an entry can be made for a draft drawn in a foreign currency the amount is converted into its dollar value at the rate of exchange for that day. This converted value is recorded in the journal entry, as well as the amount of the draft in foreign currency.

The facts that drafts are drawn in currencies other than that of the United States; that sales are made in currencies other than dollars, and that the company has more or less funds on deposit in foreign countries at all times, make it necessary to have some of the ledger sheets double-ruled so that both currencies can be recorded in all cases where necessary, such as foreign bank accounts, agents' accounts, foreign customers' accounts, draft accounts, advances, etc.

Upon the payment of the shipper's accepted drafts, the same kind of entry is made as for the payment of drafts drawn by the company's travelers, except in the case of drafts drawn in foreign currencies. The latter are paid at the rate of exchange of the day of payment and this rate will vary more or less from the rate at which the drafts were originally entered in the unpaid-drafts account. In order to balance the account a further entry is necessary, debiting or crediting the unpaid-drafts account with an amount equal to the difference between the original conversion value and the amount actually paid to the bank with a corresponding amount credited or debited to a foreign-exchange-difference account, as the case may be.

A purchase account is kept in the general ledger for each class of merchandise, to which are debited all purchases of the respective class of goods, transfers from manufacturing accounts and transfers from storage accounts. These entries are made in totals monthly. All purchases of merchandise are recorded in a merchandise-purchase register and the monthly closing entry for this register is as follows:

Merchandise purchases (class 1)...... Dr.	
Merchandise purchases (class 2)...... Dr.	
Merchandise purchases (class 3)...... Dr.	
Merchandise purchases (class 4)...... Dr.	
To Accounts-payable account	Cr.

After recording the purchase in the purchase register the items from domestic sources are paid for by cheque and accounts-payable account is debited with the amount by the customary monthly closing entry of the cheque register. In the case of purchases made by company's travelers, the accounts-payable account is cleared by journal entry, as follows:

Accounts-payable account........... Dr.	
To Importation-advance account	Cr.

Where shippers have drawn for only a portion of the value of the goods, an entry is made as above, thereby clearing the importation-advance account for the amount of the draft paid, and the remaining portion is entered through the cashbook, thereby completing the clearance of accounts-payable account.

The company's manufacturing accounts do not differ from those of many other concerns and they are not of importance in the present instance, except that the transfers of finished products from the factory to stock are summarized monthly and the respective merchandise-purchase accounts are debited with the total output of the factory during the month, valued at cost.

In the company's general ledger there is a control account for merchandise in storage. This account represents the value of merchandise which the company has found it necessary to hold in public warehouses, through the lack of storage space at its plant. A subsidiary ledger is kept for this merchandise containing a record of each lot stored. A record of all transfers to storage is kept in a special binder from which the necessary postings are made to the subsidiary storage ledger during the month. This binder is summarized monthly and a monthly closing entry is posted to the general-ledger accounts as follows:

Merchandise-in-storage account......Dr.
  To Merchandise purchases (class 1)..............Cr.
    Merchandise purchases (class 2)..............Cr.
    Merchandise purchases (class 3)..............Cr.
    Merchandise purchases (class 4)..............Cr.

Returns of merchandise from storage to stock on hand are handled like the transfers to storage, except that the monthly closing entry is the reverse of the foregoing entry:

Merchandise purchases (class 1)......Dr.
Merchandise purchases (class 2)......Dr.
Merchandise purchases (class 3)......Dr.
Merchandise purchases (class 4)......Dr.
  To Merchandise-in-storage account   Cr.

A separate binder is kept for the transfers of merchandise to merchandise-consignment account and a monthly closing entry is made similar to the one used in the closing of the to-storage binder, except that the debit is to merchandise-consignment account. Further reference will be made to the handling of these consignment stocks.

In addition to the above entries to the respective merchandise-purchase accounts, there will be the usual entry for returned purchases. A monthly entry will be posted to the credit of the account, transferring to the export department the cost of the merchandise sold direct from stock by that department during the month. At rare intervals consigned goods are returned and in such cases the transaction is recorded through the general journal, debiting the correct merchandise account and crediting consignment account.

Summarizing the foregoing transactions on the various merchandise accounts, the monthly entries are as follows:

Debits	Credits
Purchases	Return purchases
Transfers from manufacturing accounts	Transfers to storage
Returns from storage	Transfers to consignments
Returns from consignments	Transfers to export department

Inasmuch as all transfers are made at cost prices and inventories are priced on the same basis (or, in case the inventory of goods on hand is valued at prices lower than original cost price, a further journal entry is made debiting inventory-adjustment account and crediting the proper merchandise-purchase account with the difference in valuations) by debiting the accounts with the inventory on hand at the beginning of the period and crediting the account with the inventory on hand at the end of the period, the account shows the cost of domestic sales for the period.

The manner in which the company handles its domestic sales and returns and allowances is not of particular interest at this time, except that a sales account is kept for each class of merchandise handled so that at the end of each month or period the net sales of each class of merchandise are shown by the trial balance.

The company has at all times more or less merchandise on consignment to dealers and agents in foreign countries. Until an account sales is received, the value of the consigned merchandise is carried on the company's books in the consigned-merchandise account. The original entry to this account is the transfer of the cost of consigned merchandise from the merchandise-purchase accounts, as previously described in relation to the credits to the merchandise-purchase accounts.

The subsidiary ledger is a loose-leaf book. A page, or more if necessary, is assigned to each consignment. This page is started in the first instance in the export-sales department, when the original order is given to the shipping department. The upper half of the page is reserved for the recording of all information regarding terms, quantities, etc. It is specially ruled, with space for all instructions given to the shipping department in reference to name and address of consignee, package marks, routine, etc.; all terms upon which the goods are to be handled by the consignee; insurance rates and amounts; and drafts to be drawn—number, rate, amount, etc. This information is all recorded on the sheets before they are turned over to the accounting department by the export-sales department. When the sheets are received in the accounting department, they are entered in a subsidiary ledger and given a consignment number.

As the goods are shipped, they are billed as consigned goods. From the office copies of this billing the accounting department records on the original ledger sheet such further information as the packages actually shipped, identifying package numbers, units or weights contained in each package, etc. The record in the subsidiary ledger now becomes the stock account for this class of merchandise as well as part of the financial records. The lower half of the sheet is ruled for debits and credits as follows: Date—Remarks—Folio—Foreign currency—Exchange rate—American currency.

The next step is to debit the respective consignment accounts with the cost of the merchandise consigned, which corresponds with the credits to the respective merchandise-purchase accounts. The totals of these individual entries are posted to the proper control accounts monthly.

Further debits will be made to the respective consignment accounts from time to time, as they are passed through the expense-voucher register, covering such items as inland freight, ocean freight, insurance, cartage, storage, etc. These items are posted daily in the subsidiary ledger and posted to the control account in total at the end of the month when the expense-voucher register is closed.

As accounts sales are received from the consignees, the export-sales department approves them and makes out sales tickets for the amount sold, and the agent is charged with the amount due, based upon the rate of exchange of the day. Entries are also prepared crediting the agent with any further expenses he may have incurred and with his commission on the sale, and charging the amounts to the proper export-department-expense accounts. If the accounting received covers a complete consignment, the consignment account is credited with cost of goods and added charges, and the same amount is distributed to the export department's cost-of-sales and expense accounts. If the account sales covers a part shipment, only a portion of the cost and added charges is transferred, according to the relationship which the quantity of goods accounted for bears to the quantity originally shipped. These transfers are summarized and at the end of the month the consigned-merchandise account is cleared by journal entry as follows:

Cost of export sales (class 1) .... Dr.	
Cost of export sales (class 2) .... Dr.	
Cost of export sales (class 3) .... Dr.	
Cost of export sales (class 4) .... Dr.	
Export department expense accounts (distributed)	
To Consigned merchandise account	Cr.

Summarizing the entries to consigned-merchandise account each month we have:

Debits	Credits
Cost—Transfers from merchandise-purchase accounts 1-2-3-4	Transfers to cost of export sales
Added charges	Transfers to export department Expense accounts

The balance on the account represents the original cost, plus added charges to date, of the unaccounted-for consigned merchandise.

In addition to the sales of consigned goods, the export department makes direct sales both on the basis of dollar exchange and foreign exchanges. These direct sales are invoiced in regular billing and posted to the debit of accounts receivable, and the respective sales accounts are credited. If the sale is in a foreign currency, the amount of such currency as well as the dollar value based upon the rate of exchange for that day is debited in the customer's account.

The cost price for each sale is recorded and summarized at the end of the month, when the totals are journalized as follows:

Cost of export sales (class 1) .... Dr.	
Cost of export sales (class 2) .... Dr.	
Cost of export sales (class 3) .... Dr.	
Cost of export sales (class 4) .... Dr.	
To Merchandise-purchase account (class 1)	Cr.
Merchandise-purchase account (class 2)	Cr.
Merchandise-purchase account (class 3)	Cr.
Merchandise-purchase account (class 4)	Cr.

We have reviewed in a general way the manner of recording the purchase of merchandise, its treatment in the accounts while in the control of the company and finally the sale. There remains the matter of collection of the accounts receivable.

All foreign accounts receivable, arising through the sale of merchandise, are kept in a foreign-customers' ledger and as already mentioned, the ruling of the sheets in this ledger is such as to allow the recording of the amount of the sale in American and foreign currency.

When merchandise is consigned, the general practice is to draw against the consignee for a percentage of the value of the goods. In case of direct sales, drafts are usually drawn against the customer at 60 to 90 days' sight for the full value of the invoice.

The amounts of these drafts are debited to drafts-receivable account and the corresponding amounts are credited to advances-on-consignments account, if drawn, against the agent to cover part value of consigned goods, and to the credit of accounts receivable when drawn against a customer. When the drafts are drawn in a foreign currency the same general rule of valuing in dollars at the rate of exchange of the day applies.

As the drafts are deposited in the bank account or sold, they are credited to drafts-receivable discounted. When notification of the payment of the drafts is received, a journal entry is made debiting drafts-receivable-discounted account and crediting drafts-receivable account. These entries clear the accounts as far as sales to customers are concerned.

In the case of accounting by agents, after crediting the proper sales accounts, as reported in the account sales, and debiting the agent's account, there is open on the books an account receivable due from the agent for the amount of the sale, less his expenses and commissions, and a credit balance in advances-on-consignment account for the amount of the draft drawn against the shipment. To clear the advance account, an entry is made debiting the advance account and crediting the amount to the agent's account. If the agent has remitted the balance due, this amount is credited to his account and the account will be in balance, as far as the foreign currency is concerned, and a further entry transferring the balance in dollars to foreign-exchange differences will adjust the account. In many instances the agent does not remit direct for any balances that may be due the company, but deposits the amount due in some designated bank for the account of the company. In that case, a journal entry is made debiting the foreign bank and crediting the agent's account.

These bank accounts are kept in foreign and domestic values. Entries are based upon the actual foreign currency converted into dollars at the current rate of exchange at date of entry. In the case in mind, the credits to these bank accounts are generally by cable transfer, although in rare instances cheques are used. At the end of any accounting period, these accounts are valued in dollars at the rate of exchange then prevailing and the difference is adjusted through foreign-exchange-difference account.

The JOURNAL *of* ACCOUNTANCY

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A. P. RICHARDSON, *Editor*

EDITORIAL

Twenty-fifth Year of Publication

In November, 1905, the first issue of THE JOURNAL OF ACCOUNTANCY was published under the auspices of the American Association of Public Accountants. In November, 1929, therefore, the magazine enters upon its twenty-fifth year of continuous publication. Today, THE JOURNAL is owned by the American Institute of Accountants, successor to the American Association of Public Accountants, and is published by a subsidiary publishing company. At the end of the twenty-fifth year it will be of interest to review the accomplishments of the profession during what will doubtless prove to have been the most important quarter-century in the history of the profession in this country, for it is the period during which the profession has advanced most rapidly toward its proper position in public estimation. At the moment it is of interest to consider the continuity of publication of this magazine. Nowadays magazines come, and a good many of them go. Those that have a real purpose to serve abide, at least for a time, and we believe it may be regarded as proof positive of the enduring usefulness of THE JOURNAL that it has continued without intermission through all these years—its business under various forms of control but its policy always to stimulate the advancement of the profession under direction of the national organization. Every magazine publisher is aware of the great changes which have taken place, especially during the past ten years, in the habits of the public. Radio and the automobile are said to have done more to reduce reading than any other two factors in modern history. Today the tired business man and his equally tired wife and family find the evening a time for listening to the outpourings of a dozen radio stations, or, if the weather be fine, the evening is spent touring the countryside. Magazines are not read as they were in the last generation. Some of the oldest and best loved have passed out of existence and others are reducing the number of their issues. All sorts of devices are employed to maintain circulation by encouraging present subscribers to continue or by bringing in new ones. Gifts, which are usually described as premiums, are offered to encourage subscription, and special prices are quite the order of the day. Through all this period of transition THE JOURNAL OF ACCOUNTANCY has pursued the even tenor of its way, has never offered any special inducement to subscription (except a slightly reduced rate to college students, which was established for the purpose of making the subscription easier for men and women who had not yet reached full earning capacity), and it has been the fixed policy of the magazine to make its circulation figures always absolutely truthful and frank. Today the circulation is a cause for considerable gratification, for, while there has been a decline at times, the actual average, paid circulation remains on a fairly constant level. Various methods of increasing apparent circulation, such as carrying subscriptions beyond their termination, have never met with favor in the business offices of this magazine. These comments upon the progress and policy of the magazine are made for the purpose of demonstrating that a technical magazine can survive without adventitious aid. It may be added with a spirit of pardonable pride that throughout the time of THE JOURNAL'S publication under the auspices of the Institute it has brought in a fair amount of profit to the organization. During the fiscal year of the Institute which ended August 31st The Journal of Accountancy, Incorporated, reported an operating profit more than twice that of the preceding fiscal year.

An International Congress on Accounting

During the week beginning September 9th a "congress on accounting" was held in New York. The men and women attending the congress were, naturally, chiefly from the United States, but there was a fairly representative number of visitors from European and other foreign countries. The sessions were well attended and the various entertainment features seemed to meet with cordial favor. The congress was not conducted by any organized body of accountants but several organizations, among them the American Institute of Accountants, were represented on the executive committee. The persons present were not all professional practitioners. There were many cost accountants and representatives of schools of commerce and the like, but the subjects discussed were of interest to all to whom the word accounting has significance. The congress was really the third international gathering of its kind. The first was held at St. Louis at the time of the World's Fair in 1904. The second was held at Amsterdam in 1926. An effort is to be made to assure the repetition of international gatherings in the future. Probably the actual benefits of these gatherings are largely social, but it seems inevitable that from a meeting of men engaged in similar vocations throughout the world there must arise much good to the entire accounting field. Some important and valuable papers were presented and discussed. Their number precludes reproduction in full, but the report of the proceedings is to be published in book form and will doubtless constitute a noteworthy addition to the literature of accountancy.

Institute's Annual Meeting

Partly as a result of the international congress on accounting and partly because of the constantly increasing fellowship between professional practitioners in the English-speaking countries, the annual meeting of the American Institute of Accountants, which occurred in the week beginning September 15th, was attended by more representatives from other lands than ever before. Most of the Canadian and British societies were represented by several members and many of them took an active interest in the discussions. The meeting was altogether delightful and helpful. The papers, some of which appear elsewhere in this issue of THE JOURNAL OF ACCOUNTANCY, dealt with timely topics. The meetings were characterized by the utmost enthusiasm.

Trend Toward Business Mergers

Newspapers and magazines throughout the country are discussing the growing tendency toward amalgamation of business enterprises. In the last decades of the nineteenth century there was a strong trend toward the creation of trusts. A trust was supposed to be a group of businesses under one head and maintaining a monopoly of the production of some article or class of service. The famous Sherman anti-trust act of July 2, 1890, was intended to prevent the over-centralization of business control and to protect the public from the extortions which monopolies may exact. The country passed then into a period of business individualism and anything which savoured of a large combination was looked at askance. People feared the penalties of the Sherman act, and for a time public sentiment demanded rigid abstinence from amalgamation. But in the present century, and especially since the war, there has been a reaction and today we are running fast toward a condition of centralization which will far exceed the most highly organized efforts of forty years ago. Following the war came enormous increases in the scale of wages paid to labor; the cost of commodities required in manufacturing or in merchandising advanced with startling rapidity; and it became necessary to effect economies wherever possible. The most assailable element of expense seemed to be in management and other overhead, and the simplest way for a business to reduce cost of production appeared to be by letting one overhead cost do the work of two or more. In other words, there was an almost universal effort to consolidate for the purpose of eliminating executive and similar expenses. The result of this tendency was a substantial increase in the ratio of profit in most cases and, consequently, businesses in which mergers had not taken place began to regard with favor consolidation in their own fields. Public utilities have been grouped so rapidly and enormously that the public is hardly aware yet of the extent to which a few corporations practically control the power, fuel and light supply of the country. In some great basic industries such as transportation, the only brake upon the progress of consolidation has been the interference of regulatory commissions, but the tendency can not be checked until it has been demonstrated to be unsound. So far the movement toward mergers has been accelerated month by month.

Accountants Seriously Affected by Mergers

Now all this is of immense importance to the practising accountant because, when any two companies become one company, two audits become one audit—and the great bulk of professional service rendered by the accountant is in the arena of audit. In many cases mergers have absorbed scores of separate entities and the effect has been almost disastrous to many accounting practitioners. At least that is the way some members of the profession describe the existing conditions. And it is undoubtedly true that the present trend toward amalgamation of business has borne very heavily upon members of the accounting profession, but the so-called small practitioner is not the only one who suffers. Many of the largest firms have lost important clients whose business has been taken into some vast consolidation. The large firms, however, are usually better able to bear the loss of a client or a dozen clients than a man whose practice is comparatively small, and we may take it, therefore, that the adverse effect of mergers is more keenly felt by the individual practitioner or the moderately small firm.

Accountants' Opinions on the Subject

This is a subject upon which there is, of course, great difference of opinion and it would be eminently desirable if there could be an open discussion of the whole question from every point of view. In such a discussion there should be ample opportunity for the presentation of the views of the large firm and the small. It is quite possible that some accountant who has lost a dozen desirable clients because of the present trend of business will regard with a certain amount of skepticism any profession of regret on the part of the large firm which has benefited by the diversion of an audit engagement. It must be remembered, however, that much of the loss in the volume of professional engagements is an absolute loss to the profession as a whole. Many mergers which have taken place have not simply transferred the volume of accounting service from one firm to another. They have actually reduced the volume. At a recent meeting of the New England region of the American Institute of Accountants and the Massachusetts Society of Certified Public Accountants, George O. May, senior partner of one of the largest firms, discussed the question of mergers and it is desirable to quote his remarks on this subject. Probably his opinions may be regarded as fairly reflecting the views of many of the more prominent accounting firms. He said in part:

> "There is one tendency in modern corporation development that I would like to speak on especially—that is the tendency toward mergers and consolidations throughout the country. I suppose it is an economic development that can hardly be arrested, but it brings in its train a great many unfortunate consequences, as I suppose is true of all important economic changes.
>
> "I can not view without regret the elimination of so many independent business men throughout the country or their being forced to choose between accepting the position of salaried employees and being forced out of business altogether, though this is an inevitable incident of this development.
>
> "Another thing that I view with regret is the displacement of local auditors of these smaller concerns and their replacement by firms which

enjoy a national reputation. The relations between the national firms and the local firms have always seemed to be a question of very real importance to the profession. I have never regarded their positions as at all antagonistic. In the past, undoubtedly a certain amount of work of the local accountants has passed in the natural development of business to the national firms, but I have felt that that was far more than compensated for by the general development of accounting throughout the country, which could not have been accomplished without the national firms, and I still feel that the national firms ought to be an asset to the local firms.

"I do not think that the national firms any more than the local firms can prevent the operation of an economic force such as I have referred to. I know—speaking for my own firm—we have tried at times to do it but unsuccessfully. We have never wished to grow at the expense of the local accountants. We have encouraged our clients more than once to retain the local accountants where we felt there was reason to believe that the local accountant could render all the service that was required, but I know that, nevertheless, we and other national firms must have taken a very considerable business from local accounting firms and that the loss of that business to the local accounting firms has been far more important to them than its gain has been to us. Now, what can we do to compensate? The one thing above all that I think we should do is that every national firm should maintain a standard commensurate with its position—I fear that there are some national firms that do not, either in the ethics of getting business or in the ethics of doing business. I think it is the duty of the big firms to fight the battles for the whole profession. They can do it at much less relative cost. In order to fight these battles of principle, one has to be prepared to lose connections which carry remunerative fees or prestige that is valuable in itself. If the small firm loses an important audit, it means a substantial share of its total business—a big firm can lose a number without really feeling it. And that is why I feel that the first and foremost duty of the national firms is to take the strongest possible stand on questions of ethics and on questions of principle, and in both these fields to fight the battle of the whole profession. Now, I don't think that we are all doing it, but I think we ought to do it and I am glad of an opportunity to express myself very plainly on the subject.

"I sympathize very heartily with the local firms, which are doing good work in a professional spirit, but complain that the national firms are not always maintaining the standards of either accounting principles or ethics that they advocate and seek to impose on the profession as a whole.

"There is no doubt that there is room for both national firms and local firms in the profession and I don't think if the two work together properly that anything essentially antagonistic in their positions can develop. That it is possible to make a great success without having a national organization is obvious. I happen to be in the position of having on each side of me a man who has accomplished just that. And what they have done, others can do."

These are the opinions of a member of a large firm of accountants whose practice spreads into every part of the country and into many foreign countries. It would doubtless be of interest to many readers of this magazine if some individual practitioners—those who have suffered most from the effects of mergers—would express themselves with equal frankness on the present trend toward mergers. We invite comment of this kind and trust that it will be forthcoming and will be on a plane of high professional thought. Personal feelings may influence the writers' thoughts but should not influence their writings. There is no more important question which can engage the attention of an accountant.

Accountants and Legal Knowledge

THE JOURNAL OF ACCOUNTANCY receives a good many letters in the course of a year asking for advice as to the desirability of a knowledge of law by accountants. Most of the correspondents are young men who have acquired a certain amount of knowledge of accounting, especially theory, and are anxious to increase their usefulness and possible earning power by the acquisition of other kinds of knowledge which may add to their general value. The old axiom that one can not know too much about anything is not universally accepted today. There are many things which one may know without increasing his usefulness or happiness, and there is often danger that the man who seeks to know much about everything will know little about anything; but it may be said that as a rule a knowledge of law is of real value to a practising public accountant. So, too, is a knowledge of economics, mathematics and statistics. Law is desirable as a supplement to accounting knowledge. An accountant should know enough about law to know when a lawyer should be called in, but he need not be proficient in all branches of legal knowledge. It is generally believed in the profession that to be a good accountant is a job big enough for one man. To the practitioner who would make professional accountancy his life work we should say that his first duty would be the acquisition of a broad, comprehensive knowledge of accountancy. This does not mean that a study of law will not be exceedingly helpful. Papers on commercial law are included in almost all accountancy examinations. Many accountants are members of the bar, but we do not believe that there are many men who can be both good lawyers and good accountants. Either profession is sufficient to occupy the mental energies of an ordinary citizen. It would be our opinion that the man who expects to enter the profession of accountancy should first devote his attention to a study of accountancy and then to law or other subjects which may be collateral to the practice of his chosen profession. Furthermore, one who would be an accountant primarily need not enter into all branches of legal study but should limit his attention to those departments of law which relate to commerce, finance and industry.

Income-tax Department

EDITED BY STEPHEN G. RUSK

To the readers of this department we offer our apologies with profound regret for an error in the August number of THE JOURNAL OF ACCOUNTANCY, wherein it was asserted by us that a claim for refund and an assertion of a deficiency on account of a 1925 tax return could be made as late as March 15, 1930.

Our explanation of the error is that we unwittingly presumed that the 1925 income-tax was imposed under the provisions of the act of 1924, instead of that of 1926. This latter act became retroactive to January 1, 1925, and, therefore, the statue of limitations of the latter act took precedence over that of the 1924 act. Under the provisions of the 1924 act a taxpayer had four years from the statutory date of making a return within which to file a claim for overpayment, whereas the 1926 act reduced this period to three years from the statutory date of making the return.

Since the issuance of the August edition of THE JOURNAL OF ACCOUNTANCY a considerable number of letters has been received by us demanding an explanation of our palpable error, and in these paragraphs we wish to express our regret that it was made.

It seems appropriate to state that our sympathies have been invoked, because of this experience for students who are obliged to solve abstract propositions in the examinations to which they are subjected. With a concrete question before us as to a claim for refund for the year 1925, the tax return for that year would have been consulted, which would have put us on notice that it was made under the provisions of the act of 1926. However, in dealing with abstract questions as to former years' tax matters it is easy to forget the effective date of each of the several taxing laws.

In the John Doe case, our comments upon which has led to all this trouble, it appears that the taxpayer had made his claim for refund before March 15, 1929 (which was within the statutory period for making such claims) and after the claim was made and after March 15, 1929, a revenue agent appeared at the taxpayer's office and found an excessive deduction for depreciation of an amount equal to that upon which the claim for refund had been based.

Section 277 (a) (1) of the act of 1926 reads as follows:

> "The amount of income taxes imposed by this act shall be assessed within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period."

In the case of John Doe, no waiver of the statute of limitations was asked nor furnished, and, therefore, March 15, 1929, seems to have been the last date upon which any assessment for a deficiency could be made.

It is proper to state that the claim for deficiency was not filed, in John Doe's case, until March 12, 1929, and that the commissioner probably had no opportunity prior to March 15th of that year to examine the accounts of the taxpayer. Furthermore, it is presumable that if in examination of John Doe's claim for refund the commissioner found offsetting errors which canceled the amount of the taxpayer's alleged reduced income the statute of limitations could not be invoked as a bar to the correction of such errors as involved additional taxes.

It is interesting to draw attention to a number of cases where deficiencies have been the subject of contention until after the statute of limitations for refunds had expired; where not only was the asserted deficiency disallowed but an amount of deduction allowed by the board of tax appeals greater than that taken in the return, and, upon the taxpayers making claims for refund at the termination of the case, they were informed that as the period in which such claims could be made had expired, no refund could be allowed.

It is difficult for the taxpayers to comprehend why the government can find additional taxes after the statute of limitations has expired, to offset claims for refund made before such expiration, when, on the other hand, the taxpayer is estopped from collecting refunds for overpayment of taxes found in the course of contending against the assessment of a deficiency, when such assertions of deficiencies ultimately have been found to be erroneous after the expiration of the statutory period for claiming such refunds.

Robert H. Lucas, commissioner of internal revenue, was one of those kind enough to write us as to our regrettable error in the August number. We feel that all our readers will appreciate his interest in our profession in directing our attention to the correct solution of the problem presented by the case of John Doe.

It is with pleasure that we quote his letter in full:

Editor, The Journal of Accountancy

Sir: Attention is invited to the article on federal income tax appearing on pages 135 and 136 of the August, 1929, issue of The Journal of Accountancy. This article contains a criticism of the "machinery" provided in the revenue laws for the administration thereof, such criticism being based upon a discussion of the law and procedure applicable to a particular case.

The statements in the article relative to the law and procedure applying thereto are incorrect. A correct statement of the law and procedure involved in the particular case discussed is, therefore, submitted for your information.

Briefly stated the case discussed concerned a taxpayer who had omitted a certain allowable deduction from his return for 1925 and subsequently filed a claim for refund of the overpayment of tax resulting therefrom. The claim was audited by a revenue agent who found that the taxpayer had overstated another deduction by an amount equal to that omitted from the return. The net income and tax liability originally reported, therefore, were neither decreased nor increased as the result of these adjustments inasmuch as the items offset each other. Accordingly, the examining officer informed the taxpayer that no refund of tax would be made.

In the discussion of this case the article in question states the law and procedure applicable thereto as follows:

"Under the acts of 1924 and 1926, the taxpayer has until March 15, 1930, to make a claim for refund of overpayment of income tax returned for the year 1925. The commissioner has until March 15, 1930, to assess a deficiency of tax if found by him in a 1925 tax return. In view of the fact that the settlement of the question of overpayment and deficiency of tax can be made as late as March 15, 1930, it is presumed that in due course John Doe will receive from the commissioner an answer to his claim for refund.

"He will also receive from the commissioner prior to March 15, 1930, an assertion of a deficiency because of the excessive depreciation. Then he will have just sixty days within which to appeal to the United States board of tax appeals against the assessment of the deficiency. If he thus appeals he will then wait a year or two before the board gets to his case. In the meantime, the commissioner will withhold payment of the refund until the whole matter has been adjudicated by the board."

The statements that the period for filing a claim for refund of an overpayment of tax for 1925 and the period for assessment of a deficiency in the tax for such year extended until March 15, 1930 are incorrect. The statements presumably are based upon the provisions of section 281 (b) of the revenue act of 1924, under which the statutory period of limitation for filing claims for refund expired four years from the date the tax was paid, and section 277 (a) (1) of that act, under which the statutory period for making additional assessments of taxes expired four years from the date the return was filed. Inasmuch as returns for 1925 were filed in general on or about March 15, 1926, at which time either the entire tax or the first quarterly instalment thereof was paid, the statutory period of limitation upon refund and assessment for 1925 would have extended to March 15, 1930, had such provisions of the revenue act of 1924 not been repealed or superseded by the revenue act of 1926, and the statements made in respect thereto in the article would have been correct.

Returns for 1925 are, however, subject to the provisions of the revenue act of 1926, which although enacted on February 26, 1926, is retroactively effective as of January 1, 1925. Under section 284 (b) (1) of the revenue act of 1926, the period of limitation upon filing claims for refund of taxes imposed by the revenue act of 1926 is reduced to three years from date of payment of the tax. Consequently, unless subject to certain exceptions provided in the statute, such period with respect to the year 1925 expired on March 15, 1929, if the tax was paid in one sum. If the tax was paid in quarterly instalments, then such period terminates in respect of each instalment thereof on March 15, June 15, September 15, and December 15, 1929. Likewise, by section 277 (a) (1) thereof the period of limitation upon assessments is reduced to three years from date of filing the return and such period, unless extended by a form of consent or other statutory provision, expired in general on or about March 15, 1929 with respect to returns filed for the calendar year 1925.

The statements that in closing John Doe's case it will be necessary to assert a deficiency in tax as the result of the item disallowed as a deduction and that, consequently, if an appeal is filed with the United States board of tax appeals the refund of the overpayment of the tax resulting from the deduction originally omitted from the return will be held in abeyance until the whole matter has been adjudicated by the board, are also incorrect.

The statute provides that if upon examination of a return the tax liability determined by the bureau is in excess of the tax already paid, a deficiency results which may be made the subject of an appeal to the United States board of tax appeals. The board then has jurisdiction to decide all issues and redetermine the tax liability. Its decision is final, subject, however, to review by the courts. On the other hand, if the tax liability determined by the bureau is less than the tax already paid an overpayment of tax results, which may be refunded or applied as a credit against an outstanding liability for another year. In that event, the board does not have jurisdiction to redetermine the tax liability should the taxpayer disagree with the bureau's determination. The taxpayer, however, is not without a remedy and may file a refund claim upon the disputed questions which, upon rejection by the bureau, can then be carried to the courts for adjudication. Thus it will be observed the statute does not require an assessment of a deficiency and allowance of a refund for the change in tax liability occasioned by each and every adjustment to a return but instead the "machinery" of the law is put into motion by and operates only upon the net change in tax liability resulting from all of the adjustments made with respect to the return.

Applying the foregoing to the case of John Doe, it will be noted that inasmuch as the tax liability determined by the bureau was not in excess of the tax previously paid the case could not be carried to the United States board of tax appeals for redetermination of a deficiency. Moreover, inasmuch as the tax liability so determined was not less than the tax paid the taxpayer's claim for refund could not be allowed. Consequently, in closing the case it would be necessary for the bureau merely to issue a letter in rejection of the claim for refund. The matter then would be closed unless the taxpayer did not agree with the bureau's determination of the tax liability, in which event, as already stated, the rejection of the claim gives the taxpayer the right to bring a suit in court upon the disputed issues.

Yours truly,

(Signed) ROBT. H. LUCAS,
Commissioner of Internal Revenue.

August 28, 1929.

SUMMARY OF RECENT RULINGS

Personal-service classification allowed a taxpayer conducting a produce and fruit commission business. (Circuit court of appeals, fourth circuit. *Atlantic Coast Distributors* v. *Commissioner.*)

The worthlessness of a debt is held not established where the debtor is a person of large earning capacity, owns considerable property, and has a high standing as a citizen and public officer.

A stockholder's loss on the stock of an insolvent corporation is deductible in the year the corporation is adjudged insolvent.

Failure to establish cost of stock precludes deduction of loss. (District court of the U. S., western district of Pennsylvania. *In the matter of John A. Bell, bankrupt.*)

A taxpayer on the accrual basis entitled to receive extra compensation from the employing corporation's net profits, having bound himself to invest such compensation in the corporation's stock which is to be held in trust for him during the term of his employment, should report compensation used to purchase the stock as income for the year the purchase was made. (U. S. district court, southern district of New York. *O. Victor Rodrigues, plaintiff* v. *William R. Edwards, former collector of internal revenue for the second district of New York.*)

An inventory valuation at December 31, 1917, based on "normal cost which would approximate values of 1915" is not an inventory valued at cost. (*Western Dry Goods Company* v. *U. S. of America.* U. S. district court, western district of Washington, northern division.)

An amount credited to the account of a deceased employee in consideration of his long and faithful service is held to be an ordinary and necessary business expense deductible in the year credited. (U. S. district court, eastern district of Pennsylvania. *Philip Wunderle* v. *Blakely D. McCaughn, collector.*)

A return on the calendar-year basis filed by a taxpayer keeping books on a fiscal-year basis does not start the running of the statute of limitations, which does not begin to run until a return or returns are filed which at least purport to cover the period involved, and where two returns are filed each including a part of the taxable year the statute does not run until a return or returns are filed which at least purport to cover the period involved, and where two returns are filed each including a part of the taxable year the statute does not run until it expires as to both returns. (U. S. circuit court of appeals for the ninth circuit. *Paso Robles Mercantile Company* v. *Commissioner.*)

An amount in settlement of patent-infringement claims paid to a corporation and by it distributed as dividends to another corporation, its sole stockholder, as a means of effecting the distribution to the stockholders entitled thereto, is not taxable to the second corporation, where the first corporation was legally obligated to pay the said amount to its former stockholders, the second corporation after its payment standing in the same financial condition as though the amount had been paid by the first corporation direct to its former stockholders.

(U. S. district court, northern district of New York. *Ansco Photo Products, Inc.*, v. *Jesse W. Clark, collector.*)

The payment by an employer of the income taxes assessable against an employee constitutes additional assessable income to such employee. (U. S. circuit court of appeals, first circuit. *Old Colony Trust Company, et al., executors*, v. *Commissioner.*)

Under a partnership agreement it was stipulated that a future incorporation of the business was to take place to be based on the capital invested in the business by the partners as evidenced January first previous by a private ledger to be kept by one of the partners; that one seventh of the total stock issued by the corporation was to revert to one partner; that the remaining six sevenths were to be divided between the other three partners as their interests might appear from said private ledger. Held that when subsequent to incorporation a sum was transferred on the corporation's books to cover the issuance of a one-seventh interest to the partner first mentioned, such action was proper, and that the gross estate of one of the other three partners, then deceased, should be determined without including the amount represented thereby. (U. S. district court, eastern district of New York. *DeWitt A. Davidson, as successor, etc.*, v. *John T. Rafferty, collector.*)

A waiver covering the limitation period for refund of prior year taxes paid by a corporation merged with another corporation is valid where the waiver was executed and filed by the new corporation, the merger under Pennsylvania laws being merely a readjustment of the relation of the original shareholders among themselves. (U. S. circuit court of appeals, third circuit. *D. H. Phillips, collector*, v. *The Lyman H. Howe Films Company.*)

A lessee under a lease requiring maintenance and restoration of property of a like quantity to that leased is not allowed deductions for depreciation on such property or for claimed losses on any of such property sold or otherwise disposed of at prices below the amounts itemized in the lease agreement. (U. S. circuit court of appeals, sixth circuit. *Ohio Cloverleaf Dairy Co.* v. *Commissioner.*)

A new corporation resulting from the consolidation of several corporations, having taken over the assets and assumed the liabilities of the old corporations, while technically a distinct legal entity, is to all practical intents and purposes a mere continuation of the old corporations and is entitled to the same deduction on account of amortized bond discount that one of the old corporations would have been entitled to if the reorganization had not taken place. (U. S. circuit court of appeals, fourth circuit. *Western Maryland Railway Company* v. *Commissioner.*)

The two principal stockholders of an undissolved corporation are liable as distributees under the trust-fund doctrine for unpaid income taxes of the corporation, where such stockholders have caused all the valuable assets of the corporation to be transferred to a partnership consisting of such stockholders, even though no judgment for the outstanding taxes has been obtained against the corporation and even though it is not made a party to the action for recovery from the stockholders. (District court of the United States, eastern district of Oklahoma. *United States of America* v. *Joseph Tandy Courts, et al.*)

Students' Department

H. P. Baumann, *Editor*

AMERICAN INSTITUTE EXAMINATIONS

[Note.—The fact that these solutions appear in The Journal of Accountancy should not cause the reader to assume that they are the official solutions of the board of examiners. They represent merely the opinion of the editor of the *Students' Department.*]

Examination in Accounting Theory and Practice—Part II

May 17, 1929, 1 P. M. to 6 P. M.

The candidate must answer all the following questions:

No. 4 (20 points):

From the trial balance following and accompanying data, prepare the balance-sheet of the X Y Z Company as at December 31, 1928.

Trial balance, December 31, 1928

	Dr.	Cr.
Cash in banks	$ 40,000	
Petty-cash funds	500	
Notes receivable	11,000	
Accounts receivable	75,000	
Treasury notes	65,000	
Loans on call	100,000	
Investment—A B C company	25,000	
Inventories	80,000	
Land and building	75,000	
Machinery	125,000	
Office furniture	5,000	
Goodwill	50,000	
Accounts payable		$ 85,500
Notes payable		50,000
Capital stock—first preferred		200,000
Capital stock—common		200,000
Surplus		75,000
Reserve for doubtful accounts		1,000
Reserve for depreciation—building		5,000
Reserve for depreciation—machinery		30,000
Reserve for depreciation—office furniture		5,000
	$651,500	$651,500

(1) Notes receivable discounted aggregate $30,000.
(2) Accounts-receivable account is made up as follows:
  Trade accounts—debit balances $66,000, credit balances, $1,700.
  Advances to A B C company in 1910, $10,000.
  Advances to officers (collected since December 31, 1928), $500.
  Claims (collected since December 31, 1928), $200.
(3) Trade accounts regarded as doubtful of collection, $800.
(4) Treasury notes are pledged to secure notes payable.
(5) Call loans represent temporary investment of funds accumulated to acquire new plant.
(6) Investment—A B C company (100 shares of $100 each) is at cost; market value, December 31, 1928, $45,000.
(7) Cost of land, $25,000; building, $50,000.

X Y Z COMPANY

Balance-sheet, December 31, 1928

Assets

Current assets:				
Cash:				
In banks		$ 40,000		
Petty-cash fund		500	$40,500	
Receivables:				
Trade accounts	$66,000			
Less: reserve for doubtful accounts	1,000	$ 65,000		
Advances to officers		500		
Claims		200		
Notes receivable	$41,000			
Less: notes receivable discounted	30,000	11,000	76,700	
Advance payments on merchandise purchases			2,000	
Inventories			80,000	
Treasury notes (pledged to secure notes payable—per contra)			65,000	$264,200
Call loans (temporary investment of funds accumulated to acquire new plant)				100,000
Investment in and advances to A B C company:				
Advances			$10,000	
Investment—at cost (100 shares of a par value of $100 each. Market value $45,000.)			25,000	35,000
Fixed assets:				
Land—at cost			$25,000	
Building—at cost		$ 50,000		
Less: reserve for depreciation		5,000	45,000	
Machinery (chiefly manufactured by company and set up at estimated cost)		$125,000		
Less: reserve for depreciation		30,000	95,000	
Office furniture		$ 5,000		
Less: reserve for depreciation		5,000		165,000
Goodwill				50,000
				$614,200

Liabilities and net worth

Current liabilities:				
Accounts payable			$ 87,500	
Notes payable (secured by treasury notes—per contra)			50,000	
Accounts receivable—credit balances			1,700	
Federal income taxes payable—1928			25,000	
Dividends payable January 3, 1929:				
First preferred stock		$ 3,500		
Common stock		2,000	5,500	$169,700
Contingent liability on customers' notes receivable discounted		$ 30,000		
Net worth:				
Capital stock:				
First preferred, 7% cumulative—				
Authorized—3,000 shares of a par value of $100 each	$300,000			
Unissued	100,000			
Outstanding		$200,000		
Common—				
Authorized—4,000 shares of a par value of $100 each	$400,000			
Unissued	200,000			
Outstanding		200,000	$400,000	
Surplus:				
Balance, December 31, 1928			44,500	444,500
				$614,200

(8) Machinery—chiefly manufactured by company and set up at estimated cost.
(9) Accounts-payable account includes a debit balance of $2,000, representing advance payment on merchandise.
(10) Capital stock:
First preferred—7% cumulative, authorized $300,000, par value $100 per share.
Common—authorized $400,000, par value $100 per share.
(11) Federal income tax for the year 1928, $25,000.
(12) Dividends declared in December, 1928, payable January 3, 1929:
First preferred stock, $3,500.
Common stock, $2,000.

Solution:

The following comments apply to the required balance-sheet, which appears on page 291.

COMMENTS

The accounts receivable ($75,000) shown in the trial balance should be distributed to accounts receivable—trade, advances to officers, claims and accounts receivable—credit balances. In the balance-sheet, advances to officers and claims are shown as current assets because these accounts had been collected. Accounts receivable—credit balances are considered as current liabilities.

The notes receivable discounted are shown in the balance-sheet as a deduction from the gross amount of notes receivable on hand and discounted, and also on the liability side, in short, to direct attention to the contingent liability of the company.

The amount of the reserve for doubtful accounts is shown in the trial balance at $1,000. This amount, or the amount "regarded as doubtful of collection, $800" may be used in the balance-sheet.

The fact that the treasury notes are pledged to secure notes payable is noted on the balance-sheet under treasury notes and notes payable.

Although the call loans represent a temporary investment of funds they should not be shown as a current asset, as the funds so invested have been set aside for a definite purpose, i. e., to acquire a new plant.

The investment in and advances to the A B C company are shown as permanent investments.

The cost of land and buildings is separated, and the reserves for depreciation are deducted from the assets to which they apply. The bases of the valuations of the fixed assets are stated also.

Advance payments on merchandise purchases are treated as current assets to be applied against the purchase invoices for shipments of merchandise to be made, presumably, in the near future.

Dividends declared in December, 1928, and payable January 3, 1929, are current liabilities and are so shown.

No. 5 (10 points):

From the following balance-sheets of companies A and B prepare a consolidated balance-sheet, using the figures here presented which appear on the books of the respective companies.

Criticize or make recommendations for the correction of the resulting statement, if you think any are required, bearing in mind that for purposes of local taxation, company B's books must show correct results for that company as a unit.

Company A owns 100 per cent. of the stock of company B.

COMPANY A

Buildings and machinery	$700,000	
Less: reserve for depreciation	200,000	$500,000
Investment in company B		100,000
Current assets		150,000
Advances to company B		25,000
		$775,000
Capital stock—5,000 shares (par value $100)		$500,000
Current liabilities		50,000
Surplus—free	$200,000	
Appropriated for advances to company B	25,000	225,000
		$775,000

COMPANY B

Land		$ 10,000
Buildings (at cost)	$115,000	
Less: reserve for depreciation	15,000	100,000
Additions to buildings	$ 25,000	
Less: reserve for depreciation	5,000	20,000
Current assets		10,000
		$140,000
Capital stock		$100,000
Loan from company A		25,000
Current liabilities		5,000
Surplus		10,000
		$140,000

Solution:

The auditor should recommend that the accounts of both companies be classified in sufficient detail to permit charging into separate accounts the various elements of property which differ in nature. The accounts of company "A" show buildings and machinery, but no information is given concerning the land upon which the building is situated. This land may be entirely or partly owned, or leased. If the land is owned, it should, of course, be transferred to a land account.

The trial balance of company "B" shows accounts for land, buildings (at cost), and additions to buildings, but no information is given concerning any machinery and equipment. Data regarding the building additions are desirable, if for no other purpose than to check the depreciation reserves which show an accumulated reserve of 20 per cent. as against 13+ per cent. for the buildings. As the buildings of company "B" are valued "at cost" it might be inferred that the other fixed assets are valued on some bases other than cost.

In the following consolidated balance-sheet the fixed assets of both companies are combined in one account which is called "Land, buildings and machinery." It would be permissible to substitute the supplementary statement appended to the balance-sheet for this and the combined reserve-for-depreciation accounts.

COMPANY A AND ITS SUBSIDIARY, COMPANY B

Consolidated balance-sheet—working papers—date

	Company A	Company B	Adjustments Dr.	Adjustments Cr.	Inter-company eliminations	Consolidated balance-sheet
Assets						
Buildings and machinery	$700,000			(1) $ 700,000		
Land		$ 10,000		(1) 10,000		
Buildings (at cost)		115,000		(1) 115,000		
Additions to buildings		25,000		(1) 25,000		
Land, buildings and machinery			(1) $ 850,000			$ 850,000
Current assets	150,000	10,000				160,000
Advances to company B	25,000				(A) $ 25,000	
Investment in company B	100,000				(B) 100,000	
	$975,000	$160,000			$125,000	$1,010,000
Liabilities and net worth						
Current liabilities	$ 50,000	$ 5,000				$ 55,000
Loan from company A		25,000			(A) $ 25,000	
Reserves for depreciation				(2) $ 220,000		220,000
Buildings and machinery	200,000		(2) 200,000			
Buildings		15,000	(2) 15,000			
Additions to buildings		5,000	(2) 5,000			
Capital stock:						
Company A	500,000					500,000
Company B		100,000			(B) 100,000	
Surplus				(3) 210,000		210,000
Company A	200,000		(3) 200,000			
Appropriated for advances to company B	25,000					25,000
Company B		10,000	(3) 10,000			
	$975,000	$160,000	$1,280,000	$1,280,000	$125,000	$1,010,000

Because of insufficient information, it is assumed that the investment of $100,000 represented the book value of company "B" at the date of its purchase by company "A," and that the surplus of $10,000 shown in the balance-sheet of company "B" represents its earnings since the date of purchase.

If financial statements were necessary for purposes of local taxation, those of company "B" should be used, and not the consolidated balance-sheet.

Working papers appear on page 294.

COMPANY A AND ITS SUBSIDIARY, COMPANY B

Consolidated balance-sheet—date

Assets

Current assets			$160,000
Land, buildings and machinery (see below)		$850,000	
Less: reserves for depreciation		220,000	630,000
			$790,000

Liabilities and net worth

Current liabilities			$ 55,000
Net worth:			
Capital stock (5,000 shares, par value $100 each)		$500,000	
Surplus	$210,000		
Appropriated for advances to company B	25,000	235,000	735,000
			$790,000

Available data of fixed assets and reserves for depreciation:

	Company A	Company B	Reserve for depreciation	Carrying value
Land		$ 10,000		$ 10,000
Buildings (at cost)		115,000	$ 15,000	100,000
Additions to buildings		25,000	5,000	20,000
Buildings and machinery	$700,000		200,000	500,000
Totals	$700,000	$150,000	$220,000	$630,000

ILLINOIS EXAMINATION QUESTION

The following is an estate problem given by University of Illinois, board of examiners in accountancy, in the examination in theory of accounts and practical accounting, part II, November 23, 1928:

Problem:

The books of the Prestigo Estate were audited for the year ending October 31, 1927, by certified public accountants. Their balance-sheet at that date, which follows, was found by you to agree with the books.

PRESTIGO ESTATE

Balance-sheet, October 31, 1927

Assets

Cash—income account	$ 15,146.25
Cash—estate account	6,498.11
Notes receivable	10,050.00
Investments in stocks	385,256.20
Investments in bonds	188,334.82
Investments in real property	67,431.51
Prepaid insurance	10.86
Furniture and fixtures (less depreciation reserve $856.20)	2,510.01
Total assets	$675,237.76

Liabilities and net worth

Due income beneficiary	$ 15,146.25
Accounts payable	586.01
Estate account—value at death in 1913	464,965.22
Net income to April 30, 1926	201,555.17
Net loss—fiscal year 1926–27	7,014.89*
	$675,237.76

* Red.

Shortly after October 31, 1928, you are called in to conduct the audit for the fiscal year 1927–28. You find that the annual audit is provided for in the will and is to be paid from principal. The will also provides that principal and income are to be distinguished according to the usual custom in estate accounting; namely, that profits or losses from the disposition of assets belong to principal rather than income. However, the will directs that depreciation on rented real estate be charged against the income therefrom. Your investigation leads you to conclude that the balance-sheet prepared last year is correct.

Wilberta Prestigo is the life tenant and one of the two trustees appointed by the will, the other being J. Burton Wade, the family counselor. It is mutually understood between the two trustees that Mrs. Prestigo shall have the books of account kept under her direction and that Mr. Wade's responsibility will be met by having reliable auditors review the books of account each year. The arrangement has remained thus since 1913, when Mr. Prestigo died. At October 31, 1928, you find the trial balance to be:

Account	Debit	Credit
Cash—First National Bank	$ 5,265.23	
Cash—Central Trust Company	872.56	
Cash—Sheridan Trust & Savings Bank		$ 247.10
Notes receivable	22,475.00	
Investments—stocks	329,004.60	
Investments—bonds	176,169.82	
Investments in real property	134,757.01	
Prepaid insurance	14.22	
Furniture and fixtures	3,366.21	
Reserve for depreciation of furniture and fixtures		1,024.50
Due income beneficiaries October 31, 1927		15,146.25
Accounts payable		586.01
Estate account		659,505.50
Dividends received		13,670.00
Interest received		10,225.00
Rents received		18,667.18
Rent expense (including depreciation and insurance)	7,363.93	

Account	Debit	Credit
Worthless securities	$ 8,251.60	
Office expenses	385.10	
Depreciation—furniture and fixtures	168.30	
Real-estate taxes	586.01	
Payments to income beneficiary—November 18, 1927	15,146.25	
May 25, 1928	15,245.70	
	$719,071.54	$719,071.54

Cash deposits have not been separated as between principal and income.
Notes receivable at October 31, 1927, consisted of:

Demand loan to Wilberta Prestigo (no interest charged)	$10,000.00
Curto Patex—a lessee—note covering past-due rent...	50.00
Total at October 31, 1927	$10,050.00

During 1927–28, Mrs. Prestigo withdrew additional funds from the estate and gave additional non-interest-bearing demand notes amounting to $12,450. Curto Patex paid $25 on his note.

Two changes occurred in the stocks during the fiscal year 1927–28. Two hundred and forty shares out of four hundred fifty shares of Pasquinade Motor Company common were sold for $48,000.00, the details following:

Date of acquisition	No. of shares	Value at death	Selling price	How acquired
1913	240	$24,000	$48,000	At death
1913	60	6,000		At death
1916	150			Stock dividend of 50%

Stock of the Dejected Oil Sales Company was written off as worthless; it had cost $8,251.60 in 1915.

Twelve $1,000 bonds which had been purchased in 1920 at par were r edeemed at 101 and accrued interest of $45.00.

At October 31, 1927, real-estate investments consisted of:

Business property (at cost less depreciation)	$52,765.88
Prestigo family residence (value at death)	14,665.63
Total at October 31, 1927	$67,431.51

An addition of $68,525.50 is accounted for by the fact that in January, 1928, a contract for the purchase of a certain business corner was entered into, the total consideration being $268,000. Title was taken in the name of Prestigo Building, Inc., a building corporation, and stock of 2,678 shares was issued to the estate, one share to Mr. Wade, and one share to Fortescue Prestigo, a total of 2,680 shares, which was the authorized issue. One fourth of the purchase price was paid down and $1,525.50 was paid for legal and transfer fees; the balance is represented by a first mortgage of $134,000 due in full April 1, 1935, and seven notes, maturing serially, beginning with April 1, 1929, the first for $7,000 and the balance for $10,000 each, interest at 6% payable semi-annually. The notes are endorsed personally by Mrs. Prestigo, as trustee, although the building corporation is the maker, and are further secured by certain stocks belonging to Mrs. Prestigo. In the will creating the trust, you find, among other provisions:

". . . and at no time shall more than twenty per cent. (20%) of the assets of said estate consist of real-estate investments . . ."

Trustee Wade informs you that his signature, as trustee, has not yet been secured on the mortgage or on the notes, but asks you to prepare your statements as though he had done so, appending such qualifications as you deem necessary. Depreciation on rented properties, credited directly to the asset account, was $1,200 for 1927-28, and has been charged to rent expense.

In past years depreciation on furniture and fixtures has been divided equally between principal and income. The same division has been made of office expenses. Federal taxes apply only to principal, since all current income is distributed; local taxes are charged to both principal and income on the basis of ¾ and ¼, respectively. This proration seems fair.

Local taxes now due and not expressed on the books total $610.24; accrued federal taxes on principal income are $1,249.74.

Prepare, from the above information, (1) a balance-sheet, (2) a statement of cash receipts and disbursements in which principal and income are distinguished, (3) a working trial balance on which columns for beneficiary's income, estate income and balance-sheet appear, and a list of explanations accompanying the adjustments which you deem necessary. In case a certificate is asked for, what qualifications will be necessary?

Solution:

Following are explanatory entries indicated in the working papers on page 299.

Explanatory adjusting entries

(1)

Investments—stocks		$32,000.00	
Gain on realization			$32,000.00
To record gain on sale of 240 shares of stock of Pasquinade Motor Company.			
Selling price 240 shares	$48,000.00		
Cost of stock sold—240/450× $30,000 (cost of the 450 shares)	16,000.00		
Gain on sale of stock	$32,000.00		

(2)

Investments—bonds	165.00	
Interest received		45.00
Premium on bonds redeemed		120.00
To record the interest received and the premium on bonds redeemed.		

(3)

Investment in Prestigo Building, Inc.	268,000.00	
Prestigo Building, Inc.		268,000.00
To record the investment in Prestigo Building, Inc.		

(4)

Prestigo Building, Inc.	68,525.50	
Investments in real property		68,525.50
To transfer one fourth of the purchase price ($67,000) and legal and transfer fees ($1,525) paid on account of Prestigo Building, Inc., and charged to investments in real property.		

Prestigo Estate

Working papers—October 31, 1928

	Trial balance Dr.	Trial balance Cr.	Adjustments Dr.	Adjustments Cr.	Beneficiary's income Dr.	Beneficiary's income Cr.	Estate income Dr.	Estate income Cr.	Balance-sheet Assets	Balance-sheet Liabilities
Cash—First National Bank...	$ 5,265.23	$	$	$	$	$	$	$	$ 5,265.23	$
Cash—Central Trust Company	872.56								872.56	
Cash—Sheridan Trust and Savings Bank................		247.10								247.10
Notes receivable............	22,475.00			(7) 22,450.00					25.00	
Investments—stocks.........	329,004.60		(1) 32,000.00						361,004.60	
Investments—bonds.........	176,169.82		(2) 165.00						176,334.82	
Investments in real property...	134,757.01			(4) 68,525.50					66,231.51	
Prepaid insurance...........	14.22								14.22	
Furniture and fixtures.......	3,366.21								3,366.21	
Reserve for depreciation of furniture and fixtures.........		1,024.50								1,024.50
Due income beneficiaries Oct. 31, 1927.................		15,146.25	(8) 15,146.25							
Accounts payable...........		586.01	(10) 586.01							
Estate account.............		659,505.50								659,505.50
Dividends received.........		13,670.00				13,670.00				
Interest received...........		10,225.00		(2) 45.00		10,270.00				
Rents received.............		18,667.18				18,667.18				
Rent expense (including depreciation and insurance)......	7,363.93				7,363.93					
Worthless securities..........	8,251.60						8,251.60			
Office expenses.............	385.10				192.55		192.55			
Depreciation—furniture and fixtures..................	168.30				84.15		84.15			
Real-estate taxes...........	586.01			(10) 586.01						
Payments to income beneficiary—										
Nov. 18, 1927............	15,146.25			(8) 15,146.25						
May 25, 1928............	15,245.70			(9) 15,245.70						
Gain on realization..........				(1) 32,000.00				32,000.00		
Premium on bonds redeemed..				(2) 120.00				120.00		
Investment in Prestigo Building, Inc.................			(3) 268,000.00						268,000.00	
Prestigo Building, Inc........			(4) 68,525.50	(3) 268,000.00						199,474.50
Local taxes................			(5) 610.24		152.56		457.68			
Federal income taxes........			(6) 1,249.74				1,249.74			
Accrued local taxes..........				(5) 610.24						610.24
Federal income taxes payable..				(6) 1,249.74						1,249.74
Demand loan—Wilberta Prestigo.....................			(7) 22,450.00						22,450.00	
Due income beneficiaries Oct. 31, 1928.................			(9) 15,245.70						15,245.70	
Beneficiaries' income.........					34,813.99					34,813.99
Estate income..............							21,884.28			21,884.28
	$719,071.54	$719,071.54	$423,978.44	$423,978.44	$42,607.18	$42,607.18	$32,120.00	$32,120.00	$918,809.85	$918,809.85

(5)

Local taxes	$ 610.24	
Accrued local taxes		$ 610.24
To record accrued local taxes now due.		

(6)

Federal taxes on income	1,249.74	
Federal income taxes payable		1,249.74
To record accrued federal taxes on income.		

(7)

Demand loan—Wilberta Prestigo	22,450.00	
Notes receivable		22,450.00
To transfer demand loans of Wilberta Prestigo.		

(8)

Due income beneficiaries—Oct. 31, 1927	15,146.25	
Payments to income beneficiary, Nov. 18, 1927		15,146.25
To transfer payment of Nov. 18, 1927, to liability account.		

(9)

Due income beneficiaries—Oct. 31, 1928	15,245.70	
Payments to income beneficiary—May 25, 1928		15,245.70
To record payment of May 25, 1928, as advance against the amount due beneficiary at Oct. 31, 1928.		

(10)

Accounts payable	586.01	
Real-estate taxes		586.01
To transfer payment of real-estate taxes to liability account.		

No definite rule can be laid down in respect to any gain or loss on assets purchased by the trustee. In this solution the loss on the stock of the Dejected Oil Sales Company, purchased in 1915 for $8,251.60, was charged against the estate income, and the gain arising from the redemption of the bonds purchased in 1920 was credited to that income.

The estate income as shown in the working papers may be checked by computing the amount of federal taxes, which is given in the problem as $1,249.74.

Estate income, per working papers	$21,884.28
Add: income taxes deducted	1,249.74
Income, before taxes	$23,134.02

	Amount	Tax
Net income	$23,134.02	
Less exemption	1,500.00	
Balance	$21,634.02	

	Amount	Tax
Amount taxable at 1½%	$ 4,000.00	$ 60.00
Amount taxable at 3%	4,000.00	120.00
Amount taxable at 5%	13,634.02	681.70
Total	$21,634.02	$ 861.70
Surtax—		
On	$22,000.00	320.00
On	1,134.02	68.04
Total	$23,134.02	$1,249.74

PRESTIGO ESTATE

Balance-sheet, October 31, 1928

Assets

Cash—			
Income account		$ 20,855.13	
Less: overdraft—estate account		14,964.44	$ 5,890.69
Consisting of balances in:			
First National Bank		$ 5,265.23	
Central Trust Company		872.56	
Total		$ 6,137.79	
Less: overdraft—Sheridan Trust and Savings Bank		247.10	
Balance		$ 5,890.69	
Non-interest-bearing demand notes—			
Curto Patex		$ 25.00	
Mrs. Wilberta Prestigo, trustee and life tenant		22,450.00	22,475.00
Investments—			
Stocks		$361,004.60	
Bonds		176,334.82	
Real estate—business property (cost less depreciation)	$51,565.88		
Prestigo family residence, (value at death)	14,665.63	66,231.51	
Prestigo Building, Inc., stock (100% owned—see subscription per contra)		268,000.00	871,570.93
Prepaid insurance			14.22
Furniture and fixtures		$ 3,366.21	
Less: reserve for depreciation		1,024.50	2,341.71
			$902,292.55

Liabilities and estate balances

Estate account overdraft (see contra)		$ 14,964.44	
Accrued local taxes			$ 610.24
Federal income taxes payable			1,249.74
Stock subscription payable (see investment in Prestigo Building, Inc., per contra)—			
Subscription		$268,000.00	
Payments made		68,525.50	199,474.50
Due income beneficiary:			
Balance, November 1, 1927	$15,146.25		
Income for year ended October 31, 1928	34,813.99	$ 49,960.24	
Less: withdrawals		30,391.95	19,568.29
Estate account:			
Balance, November 1, 1927		$659,505.50	
Income for year ended October 31, 1928		21,884.28	681,389.78
			$902,292.55

NOTES:

The investment in Prestigo Building, Inc., represents a subscription for all the stock in the company, which has been issued to the estate, except for directors' qualifying shares. It is expected that the estate will be called upon to pay the balance due on the stock by furnishing funds to pay the company's mortgage on the building for $134,000 due April 1, 1935, and its notes which mature serially beginning April 1, 1929, the first for $7,000 and the balance for $10,000 each, interest at 6% payable semi-annually.

The notes are endorsed by Mrs. Prestigo, as trustee, and are further secured by certain stocks belonging to Mrs. Prestigo.

The trust as created by the will limited real-estate investments to twenty per cent. (20%) of the assets. The investment in the Prestigo Building, Inc., violates this provision, for the investment in this stock represents a real-estate investment.

With the footnotes suggested above appended to the balance-sheet, the auditor could give an unqualified certificate.

PRESTIGO ESTATE

Cash account, November 1, 1927, to October 31, 1928

Receipts

	Principal	Income	Together
Balances, November 1, 1927	$ 6,498.11	$15,146.25	$ 21,644.36
Received on note—Curto Patex	25.00		25.00
Sale of 240 shares—Pasquinade Motor Company	48,000.00		48,000.00

	Principal	Income	Together
Bonds redeemed	$12,000.00		$ 12,000.00
Premium on bonds redeemed	120.00		120.00
Dividends received		$13,670.00	13,670.00
Interest received		10,270.00	10,270.00
Rents received		18,667.18	18,667.18
Total receipts	$66,643.11	$57,753.43	$124,396.54
Disbursements			
Loans on notes—Mrs. Prestigo	$12,450.00		$ 12,450.00
Purchase of stock—Prestigo Building, Inc.	67,000.00		67,000.00
Legal and transfer fees	1,525.50		1,525.50
Rent expense		$ 6,163.93	6,163.93
Increase on prepaid insurance		3.36	3.36
Office expense	192.55	192.55	385.10
Real-estate taxes	439.50	146.51	586.01
Payment to beneficiary—			
November 18, 1927		15,146.25	15,146.25
May 25, 1928		15,245.70	15,245.70
Total disbursements	$81,607.55	$36,898.30	$118,505.85
Balances, October 31, 1928	$14,964.44*	$20,855.13	$ 5,890.69
Bank accounts—			
First National Bank			$5,265.23
Central Trust Company			872.56
Sheridan Trust and Savings Bank			247.10*
Total			$5,890.69

* Overdraft.

Correspondence

ETYMOLOGY OF "IMPREST"

Editor, THE JOURNAL OF ACCOUNTANCY:

SIR: I have found the definitions published by the special committee on terminology sufficiently stimulating to induce me to make some search on my own account, and I have come across some notes regarding the word "imprest" which may be of interest.

In modern parlance the word "imprest" is used only in the phrase "imprest system." This is a system the use of which is generally confined in this country to a petty-cash fund, although the term is used in certain accounts of the British government. The cashier of the fund is given a definite round sum of money from which he pays for sundry petty expenditures of which he keeps a record frequently in a columnar book. Either at fixed periods—such as a week, or a month—or when the total expenditures approach the amount originally advanced, a statement is made showing the disbursements and the accounts to which they are chargeable. A cheque is then drawn for the total amount of such expenditures and is charged to the accounts shown in the distribution, the proceeds of the cheque being placed in the fund, which is thereby restored to its original amount.

The derivation of the word is interesting, for it carries us back for some hundreds of years and gives us glimpses of the methods of our forerunners. It aids us to picture them at their work, beruffed, be-cloaked and trunk-hosed, and reminds us of those happy times when clients were both willing and able to care for the physical comfort of those auditors, for we find that in 1552 the auditors of Lanark were allowed 6s. 8d. that they "drane" and in 1568 one item reads "Ten shillings given to the audetouris in drink." The word is made up of the preposition "in"—which is common to the Latin, French and English languages and before a labial usually takes the form "im"—and "prest."

The prefix has no definite modern significance, and was originally frequently intensive only. The "prest," however, is interesting, for it brings out the original meaning of the word. It is closely allied to the modern French "prêt," a loan or advance money, and the circumflex accent suggests that in former times the word was "prest." The word "prest" still appears in English dictionaries as meaning to put out as a loan, and in old accounts it is found used in this sense, as far back as in the days of Queen Elizabeth, for in a statement of her expenses in 1552 made by "Thomas Parry, Esquyer," we find that "The said Mr. Parrye is charged with certen somes of money by him receaved and to him payd" of which the first is "The remayne with the prest of last yere." The word has remained in constant use and always suggests the idea of a sum advanced and to be returned or accounted for.

Yours truly,

A. W. B. A.

August 10, 1929.

Book Reviews

THE FINANCING OF BUSINESS ENTERPRISES, by AVARD L. BISHOP. *Harper & Bros.*, New York. 616 pages.

Any work covering the entire field of corporate finance must, from its necessarily encyclopædic nature, inevitably be compounded of two elements, distinct yet intermingled. One of these, which makes up by far the larger part of any such book, is known and undisputed fact and received opinion. The other is the author's expression of his own point of view on controversial subjects and the results of his own research work, in which lie the value and interest to the mature reader.

The compilation and arrangement of known fact and generally received opinion is, like the cat, harmless and necessary, and requires little of a writer beyond wide reading, industry and a moderately clear style, all of which the author of *The Financing of Business Enterprises* possesses.

The general plan of the book is logical, starting with the organization of business enterprises and carrying them through the various phases of promotion, capitalization (both by stock issues and the different types of borrowings), the determination and administration of net income and the procedures in failure and reorganization. So long as facts are dealt with, such as a description of legal proceedings in organization or a history and description of various sorts of corporate securities, the author does his work well, in spite of a certain diffuseness and redundancy of style and a slightly annoying tendency to qualify statements of generally accepted fact.

Chapters which illustrate particularly well the excellent way in which facts are selected and marshalled are those, for instance, on "Choosing the state in which to incorporate," "Securing the charter and getting started," "Corporate borrowing" and the chapters describing in detail the history and varieties of corporate obligations and their marketing (chapters XV to XXIII). There are some errors of fact in these chapters as, for example, a misstatement of the terms and nature of the New York state franchise tax on corporations (chapter IX), but as the book is hardly intended as a detailed guide in such matters these errors are not serious.

As soon, however, as any attempt is made by the author to deduce general principles from facts, to base any theory on them, to discuss methods and practices of corporations from the viewpoint of motives or results rather than legal requirements or, in general, to discuss matters involving accounting theory, the results become more and more unsatisfactory.

The first three chapters on organization, sole proprietorships and partnerships are an olio of loose and inconclusive thinking on subjects which should be, in the hands of a professor in a great university, of outstanding value, not only to students of business, but of philosophy and psychology as well. It is, perhaps, too much to expect a truly philosophical theory of organization to be presented, but one is hardly prepared to be told that "the gain from organization is difficult to over-emphasize" when that is the one thing in discussing modern organization that is always done and is easiest to do. The losses and weaknesses due to organization are the difficult things, not only to emphasize, but even to discover, as they are concealed and latent, while the advantages are clear and on the surface.

It is hardly worthwhile to multiply similar instances, but the following will go to show that the general statements covering the first three chapters are not unfair.

In stating the advantages of organization (p. 4) the author says, "a squad of well organized police will soon quell a mob," seemingly forgetful of the fact that it is the authority vested in the police, rather than their organization, which dominates the mob, and also that a mob with a real leader and no organization is not so easily quelled.

Speaking of wasting assets (p. 13) he says, "when the ore is all taken from the ground, the mine is exhausted and can not be replenished by mankind, for nature has been the provider of the minerals." That is not the reason the mine can not be replenished. Nature provides corn and wheat. The real distinction is that man has not yet found a method to induce nature to replenish ore. It is not impossible that it may be found, and, if it is, the whole nature of the mining industries will be changed. The author appears to think that a wasting asset is one that is not, rather than one that can not be, replenished—which is a novel conception to say the least.

In illustrating the fact that sole proprietorships are short-lived (p. 20) it is stated that under the right of eminent domain a sole proprietor's business may be taken away from him. This reasoning is faulty on two counts: first, it is the place, not the business, that is taken and, second, the same proceedings may be taken against a partnership or corporation.

These defects, disconcerting as they are, are not so serious as others which may be generally described as an incorrect statement of the motives governing certain corporate procedures and their effects, and misapprehension of the fundamentals of accounting theory and technique with consequent incorrect use and application of accounting results.

The theoretical value of a stock right is stated (p. 363) to be exactly nil. Had the author said "mathematical" value we might agree with him, for he evidently makes the mistake of dealing with figures to the exclusion of facts. When cash from rights goes into a business and is added to an aggregate of miscellaneous assets the stockholders' interest and equity may differ widely from what they were before. Of course, in discussing working capital (p. 423) the author is forced to take the opposite view.

On page 490 is again set forth the sophistical and mathematical fact that after a stock dividend the stockholder has the same fraction of the total stock that he had before. This, of course, is quite beside the mark, as it is equally true after a cash dividend. The author ignores the fact that the real change effected by the stock dividend is to remove earnings from the probability or possibility of cash distributions to the position of a permanent investment. Before the stock dividend the stockholder has an income interest in divisible earnings; after the stock dividend he has an investment.

On page 436 it is stated that "Under most circumstances and with most corporations, the selling of additional capital stock for the purpose of converting the proceeds into working capital is, to say the least, a questionable procedure." It is frequently difficult, if not impossible, to tell whether new money is put into working or fixed capital, as usually one is increased to correspond with the other. The original issue of stock must have been made in part for working capital and if it was not "doubtful" for the original issue to be made in part to provide working capital it is hard to see why a further issue should be so considered. If a new company is acquired for stock of a parent company, stock must be issued for the acquired company's working capital, a procedure not usually considered open to criticism.

Other instances, in addition to the foregoing, of the author's unfortunate tendency to academic and impracticable conclusions could be given, but these are sufficient to show the general tendency.

The best way, perhaps, to illustrate the misapprehension of the objects and purposes of accounting exhibited throughout the book is to quote what is said on "Motives promoting creation of contingent reserves" (p. 471). The author's words are: "It may be observed that the utilization of net earnings for the creation of reserves such as we have indicated is prompted, perhaps, more by the factor of caution than anything else; by the desire on the part of the management of the enterprise in question to avoid being caught napping in the face of future expenditures more or less unusual and unforeseen. Moreover, there are at least some business administrators who are fully alive to the fact that the statements furnished them by their accounting departments are not necessarily absolutely correct in every particular, even though the accounting department may be entirely above criticism. Such administrators believe that the statements of accountants, though showing in general the condition of their business affairs at any particular time, are not necessarily wholly correct or trustworthy. We do not mean by this to cast any reflection whatsoever upon accountants or upon their work, but merely to say that it does not seem that the financial statements of accountants have the exact accuracy of a scientific formula. The feeling is held by many, and with reason, that a great deal of data in accountants' reports, which they are compelled to represent by exact figures, are really a translation at times of the estimates of engineers and others, and are not in all cases figures based upon exact and scientific data. This is no fault of the accountants; it is merely a situation that they themselves have to cope with. It is probably true that, if business administrators knew beyond the shadow of a doubt that all the statements furnished by their accounting departments had a scientific exactitude, they would feel it far less necessary to create special reserves to take care of contingencies."

It would be superfluous to refute or correct such a series of half-truths, unwarranted assumptions and inconclusive arguments. It should be enough merely to state them.

Another conspicuous example of misunderstanding of accounts and their purposes occurs in chapter XXVIII. The author says "Working capital, on the other hand, in the typical instance, is not permanently invested in the enterprise. Some have aptly called it revolving or circulating capital." For this statement to have any clear meaning it must be assumed that the word "invested" is used in its ordinary sense and as used in other places by the author himself, meaning money advanced to a corporation in exchange for some sort of security, repayment of the principal sum not being expected until the dissolution of the company or at some fixed date in the not very near future. The author himself describes how capital stock, the most permanent form of security investment so far as repayment is concerned, may be sold to provide working capital (p. 436). However, he does not himself appear to take his statement seriously, and so is not really in disagreement with the long line of thinkers from Adam Smith (from whom the term "circulating capital" is apparently derived) to those of the present day, who have uniformly held that a change in form of circulating or revolving capital does not affect its investment characteristics. It is hardly necessary to prove this again in detail as most of the rest of chapter XXVIII is devoted by the author to attacking his own statement. Writing of this sort is what we should expect our professors to condemn rather than to indulge in.

Throughout the whole discussion of accounting procedure as affecting income and financial position reserves are looked at from the credit side only. Surely the important thing about a reserve is the assets from which amounts set aside may be paid, not the credit entry segregating surplus.

Lack of familiarity with practical problems is indicated by statements such as "Repairs need not be defined" (p. 467). Anyone who has attempted an analysis and revision of the repair account of a large manufacturing corporation will hardly agree that the thing is so simple.

While there is much of value in this book for the student there are some things that are positively hurtful. For the mature reader, the banker, economist or accountant there is little. The book is, in the main, academic and derivative rather than scientific and practical. It is to be hoped that our professors will not give up writing on this subject and that eventually a completely satisfactory book on corporation finance will appear.

MAURICE E. PELOUBET.

INTRODUCTION TO BUSINESS MANAGEMENT, by HERBERT G. STOCKWELL. *Harper & Bros.*, New York. 276 pages.

In these days when every boy is convinced that his ultimate earthly destiny is the presidency of a corporation, a bank or, perhaps, only the United States, it is of the utmost importance that youth should be instructed in the duties which may befall it in those later—but not much later—years, when the burdens of executive management will rest upon its shoulders. Youth can not complain that there has not been written for it a vast number of words which have covered innumerable pages and added considerably to the income of the post-office department by virtue of the circular advertisements which have been disseminated almost broadcast. At first it does not seem that one could find much new to say about the management of business. But in spite of all that has been said and written, it does appear that there has been something left unsaid. A book which has just come from the press of Harper & Brothers, written by Herbert G. Stockwell, who is an accountant of high repute, has taken up the subject of business management and discussed it in a subjective sense. One who reads the book learns how presidents are selected and how they perform their presidential duties, but above all how they and the factory manager, the sales manager, the purchasing agent, the advertising manager and all the other managers great and small think, act and feel. It will be a great help to those who read to know something of the experiences through which they will pass when they reach the top of the ladder.

There is a hopeful looking section of the book devoted to the subject of business ethics, but, frankly, it is disappointing. Business ethics is much more than the author says of it. "Now stripped of all ethical terms, ethics applied to business means plain honesty in buying and selling merchandise, operating a factory, borrowing working capital, entering into and fulfilling contracts, paying debts, and all other ordinary business transactions." Indeed, it is much more, or it should be. One may pay his debts, for example, in a highly unethical manner. A man who places an order and receives the goods for which he contracted and then delays payment until the threshold of the debtors' court is often, except in the case of inability, guilty of dishonesty. He is in effect compelling his creditor to lend him money—and to lend it without interest. Or one might draw attention to the fact that ethics involves the manner of dealing with one's competitors or the treatment of employees or any of the thousand other ways in which one's conduct reflects upon one's environment.

The author's comments upon the necessity for good appearance, manners and habits are incontrovertible, but the chapter which is headed "Luck and opportunity" lays a little too much stress upon the impotence of luck. We may call luck by a hundred different names but it is luck nevertheless, and many a man gets to the top of the tree by sheer luck when his abilities would keep him sitting on the roots. This does not mean that merit will not tell. But what about the man who jumps into the forefront of affairs because his father was a good jumper before him?

Mr. Stockwell's book is an interesting book and written from a long experience. It will do many people a great deal of good.

A. P. R.

ACCOUNTING BY MACHINE METHODS, by H. G. SCHNACKEL and HENRY C. LANG. *The Ronald Press Company*, New York. 575 pages.

MODERN OFFICE MACHINERY, by LEONARD F. FOSTER, *Gee & Company*, London. 177 pages.

Accounting by Machine Methods and *Modern Office Machinery* differ from each other in several respects, the differences being more striking than the similarities. The respective authors have purposes in mind which are reflected in the scope of the material treated and in the viewpoint of their discussion.

Schnackel and Lang have set out to discuss the advantages and practical applications of mechanical equipment in the interpretation of accounting data only. Machine methods for handling other business information and transactions are not considered at length. No specific makes of machines are mentioned or illustrated in the text, and the figures consist solely of charts, forms, records and reports prepared by mechanical accounting devices.

Foster, on the other hand, has discussed all the major classes of office machines, with the treatment of accounting equipment comprising only one chapter. Specific makes and models of machines are described in detail, and numerous pictures of them appear throughout the book. Emphasis is placed upon the mechanical construction of the equipment, rather than the types of business records prepared with their aid.

Accounting by Machine Methods comprises chapters on the various types of information and administrative functions with which accounting records deal. The following are typical chapter headings: accounts-receivable systems; instalment accounting; sales-material control; the payroll and its distribution. *Modern Office Machinery* organizes the discussion in terms of the mechanical process which each class of equipment performs, such as writing, duplicating, addressing, calculating, accounting, sorting, tabulating and time recording.

Schnackel and Lang have not hesitated to express themselves on matters of administration, organization, office procedure and general policies of business administration. In one sense their book may be looked upon as a textbook on business management, with particular emphasis on the rôle which mechanical equipment now plays in this field. Some of the chapters lead far into problems of departmental administration, particularly those on sales analysis and stock and material control. The authors appear to assume that readers are already familiar with the various types of accounting machines, or that they will investigate the proper type when the need for mechanical equipment is demonstrated.

Foster, in his work, has concentrated on the mechanical principles of the machines themselves, rather than the problems of management and the application of the machines thereto. Some attention is given to the history of the various makes and models of equipment. He assumes, apparently, that the machines will be used at the proper time and place, once their mechanical features and advantages have been explained. His work is essentially a digest of business machines, with selected illustrations of the more important types.

The scope of the book first mentioned above is affected by the fact that other American works have served in a general way to describe the types and construction of various business machines. Schnackel and Lang emphasize the administrative rather than the technological advantages of machine methods in business. Foster has provided a semi-technical treatise on modern office machinery, describing the special features of numerous makes and models.

C. Rufus Rorem.

BALANCE-SHEET VALUES, by P. D. Leake. *Gee & Co.*, London. 75 pages.

The recent reduction in the size of the paper currency notes symbolizes in a graphic manner the fact that our money has shrunk in purchasing value. If the treasury department had made this change ten years ago, it might have been credited with the idea of bringing home to a much larger class than the income-tax payers the lesson that war is very expensive and takes years to pay for, and that everyone must do some of the paying.

Sir Josiah Stamp has reproached public accountants with holding the key to much information of cardinal importance in the solution of present-day problems and with not using it themselves or allowing anyone else to use it. It is, of course, no answer to suggest that the confidential relations of accountants to their clients makes impossible the use of information regarding economic phenomena gleaned during the course of practice. Physicians and dentists are able to epitomize and impersonalize their operations and observations and to demonstrate resulting theories without offending their patients. The world needs more men with the training and viewpoint of accountants who will apply their experience and judgment to national and international financial problems.

The author of *Balance-sheet Values* in the early part of the book shows himself to be thoroughly alive to the wider problems of accountancy contained in the measurement and recording of national wealth. Mr. Leake discusses the methods of arriving at book values in commercial businesses, mines and plantations; gives a classification of industrial assets and liabilities, and distinguishes between the natures of annuities and leases.

C. S. BRISON.

SOME ASPECTS OF RATIONALIZATION, by SIR MARK WEBSTER JENKINSON, K.B.E. *Gee & Co.*, London. 36 pages.

The writer, for one, has been somewhat puzzled by the term "rationalization" which has been projected into business terminology during the past few years by British and other foreign correspondents in the commercial and financial columns of our newspapers. Reference to standard dictionaries disclosed that the word had a technical meaning in philosophy, in theology and in mathematics; and also a popular meaning, "to apply reason to." The former three being barred by their technical definitions, I was perforce driven to conclude that "rationalization" was journalese for something in the way of reconstruction or reorganization with a vague gesture toward imitation of American methods. However flattering that might be to us, it was difficult to believe that our British cousins tacitly accepted the logical implication of the popular definition of the word—i. e., admitted that British methods in business and production have been irrational. Yet that is exactly what Sir Mark Jenkinson, in his vigorous pamphlet, *Some Aspects of Rationalization*, very bluntly, and one must say courageously, asserts in one of his definitions of rationalization.

What is rationalization? According to the gospel of Sir Mark,

> (1) "Rationalization is the mobilization of the fighting forces of an industry against the attack of the foreign manufacturer. . . . It implies not merely a reconstruction of capital, a reorganization of management, a re-shuffling of plant, but a revolution in our ideas, in our mentality, in our outlook on the industrial situation" (p. 5).
>
> (2) "Rationalization is a confession of failure—a recognition of the fact that the development of industry during the past thirty years has been conducted on wrong lines" (p. 34).
>
> (3) "Rationalization of industry is the coöperative movement of those engaged in a particular industry to win back for that industry a paramount position in the world's trade, and by goodwill, good work and good brains success can be attained."

And inasmuch as Sir Mark frequently points to American methods as object lessons, we are put upon notice that rationalization is not only a compliment to us but also a threat: in short, that England proposes to fight American commercial aggression with American methods. May the best man win!

"Rationalization" is a good, mouth-filling word, almost as awesome as "the sound of that blessed word 'Mesapotawmia'!" But why tack a new meaning on an old word? Have we not such terms as "reorganization," "reconstruction," "modernization," that would express the idea as well? One would think so, but after reading this pamphlet and considering that no one of these words will cover all the far-reaching changes that Sir Mark proposes, it is perhaps necessary to admit that some all-comprehensive word is desirable, and lexicographers may well add these definitions as technical business terms.

The rationalization of an industry is to be based on three general principles, viz:

Merger—". . . the amalgamation of the kindred businesses carried on by firms engaged in the same class of trade, grouped according to their geographical situation, and the elimination of inefficient undertakings which, except in boom periods, can never produce competitively owing to bad layout, uneconomic plant, and incompetent management, and whose turnover if added to that of efficient concerns would enable the production costs of the latter to be reduced."

Financing—"Capital must be provided to erect the best and most completely equipped works, etc."

Management—"Men must be found capable of realizing the need for fighting foreign competition rather than securing a larger proportion of the home trade, etc."

Such are the general principles. The rest of the pamphlet (which by the way is a reprint of a paper read by the author before several bodies of secretaries, bankers and accountants) is devoted to details, stating expected obstacles and making suggestions and recommendations in a broad way. That the author's remarks have created a stir in British business circles is sufficiently indicated by the fact that the reprint is due to a great demand for copies of the address, which was intended originally only for private circulation—probably where it would do the most good.

In view of the O'Fallon decision (which does not decide!) American readers will be interested in Sir Mark's ideas on valuation of fixed assets. He says quite emphatically:

> "The idea that the value of the fixed assets is in direct relation to the original cost as shown by the books, less an arbitrary provision for depreciation, is one that is generally although wrongly held.
>
> "The value of the fixed assets is merely the capitalized value of the future earnings plus the scrap value of the asset."

Which sounds a bit startling, but since the context seems to show that the "value" is that to the *combine* as a basis for equitable apportionment of ownership, we need not too hastily accuse Sir Mark of heresy. Nevertheless, looking back upon the notable wrecks of American mergers which were hopefully based on this capitalized-earnings plan, we may be pardoned for doubting its wisdom, especially on reading further that goodwill based on the traditional five-years' profits is also to be added to the capitalization. Sir Mark's programme has its perils. On the other hand the success of our giant corporations, notably U. S. Steel, shows that it can be done—by showing back earnings until the "water" has been absorbed, a process hinted at in the author's suggested provisions for depreciation reserves.

This brochure is altogether a thought-provoking bit of work for British manufacturers and financiers, and American readers may at least be grateful to Sir Mark for enlightenment on the meaning of rationalization.

W. H. Lawton.

ACCOUNTANTS' WORKING PAPERS (second edition), by Leslie E. Palmer and Wm. H. Bell, *Ronald Press Co.*, New York. 319 pages.

It is six years since the original edition of *Accountants' Working Papers* was reviewed in this magazine and now, on its fresh appearance, this intellectual offspring of the authors' has followed the example of our feminine offspring, for it has during the sexennium, if one may coin a word, broadened its outlook, shortened its skirts, and grown greatly. In other words, it now treats of several subjects not included in the first edition; it has reduced the size of its pages from 11" x 8" to 8½" x 6"—both changes adding to the usefulness of the book and to the convenience of the reader—and devotes additional space to subjects previously dealt with.

The fact that revised edition is now called for reminds one of the good old English saying "Good ware makes quick markets," and I see no reason to change in any way the opinions printed in August, 1923, nor the concluding statement that the book "should be in the library of every practising accountant." During the past six years the volume has been on my own shelves and has been consulted by principals and by staff members fully as frequently as has been the most popular of its companions.

In general, the text and the examples are identical with those formerly issued, except that the date of "1922" used in the original illustrations has been changed to "1928" in the revision.

The important detail of indexing the papers is treated rather more fully; several additional pages deal with the ownership of working papers, and there are added a couple of plates, illustrating the method of recording the practice of the client in dealing with receipts, disbursements, etc., and a memorandum of points arising during the progress of an audit which may require special attention or comment.

Two valuable additions are found in chapters X and XI, dealing, respectively, with "Working papers for the preparation of tax returns" and "Working papers for re-organizations, mergers, consolidations and new financing plans."

All accountants who have had occasion to prepare tax appeals in cases where the original returns were prepared by those who, by reason of death, removal, or other cause, are not available, will place a high value on chapter X.

The present urge to merge in order to purge and emerge is country-wide, and the importance of the proper preparation and filing of working sheets in such cases is obvious, although, alas, the obvious is not always seen until too late.

The volumes in the original edition contained 193 pages of double-spaced typewriting; the revised volume contains 313 pages of close printing, or, approximately, twice as much matter as did the original. The greater part of this addition, some 85 pages, consists of a "complete set of correlated working papers" and includes working papers as completed at the close of a representative audit and also a draft of the report prepared therefrom.

There can be no doubt of the value of this addition to the student. Is it not also of value to many practitioners as forming something like a yardstick against which they can measure their own work from time to time? There is some truth in the suggestion that such a stick, fashioned by independent outside practitioners, tends to prevent many—especially those situated far from the larger business centers—from sinking in a rut which after long use becomes a grave.

In their new preface the authors show their wisdom by stating that they have limited the scope of the present work to the limits indicated by the title, that is to working papers, and have avoided discussion on theory, on procedure and on report writing. Most accountants, probably all good accountants, realize that necessity for setting limits and the great difficulty in observing them when set. The authors have been successful in their efforts in this direction and, doubtless intentionally, have not enlarged as fully as might be desirable on some of the important and basic matters, such as verification of cash and the much vexed question of inventories.

To explain the abbreviated attire referred to above—it is often difficult to place a book 11 inches in height on library shelves which are very commonly only 10 inches apart, and this leads to placing such volumes in some odd corner or laying them on their sides—in the former case they may be difficult to find when the searcher is hurried and as for the latter, a working book like a working man should sit up, or stand up, and not lie down.

The publishers have abandoned the typewriter type, which saves much space and renders it possible to make the sub-headings stand out far more clearly.

The authors recommend working sheets 8½" x 14" and they reproduce these reduced to about 4½" x 6½". As the plates are reproduced in script, the resulting words and figures—of which there are many—are often so small as to present difficulties to eyesight which is somewhat dimmed by the study of figures for a good many years past.

Walter Mucklow.

QUESTIONED DOCUMENTS (second edition), by Albert Osborn.

Any question as to the genuineness of a document, whether written by hand or typewriter, is of interest to the members of the accounting profession.

In *Questioned Documents* the author, who has had many years of practical experience as an examiner of documents of doubtful authenticity, has covered the field most thoroughly, not only pointing out specific instances of forgeries and alterations, but explaining in detail how the deception was discovered.

The author has also treated rather exhaustively the question of handwriting and also discusses thoroughly the subject of paper and ink, as well as pencil writings. The chapter on "Order or sequence of writing" and the chapters on erasures, additions, interlineations and substitutions are most interesting and instructive.

Attention is devoted to questioned typewriting, and the chapter on "A disputed-document case in court" is a liberal education in the manner of conducting oneself on the witness stand.

While this book has been written largely on individual documents, it will not be difficult for the accountant to see the application of the principle involved to books of account.

Lee J. Wolfe.

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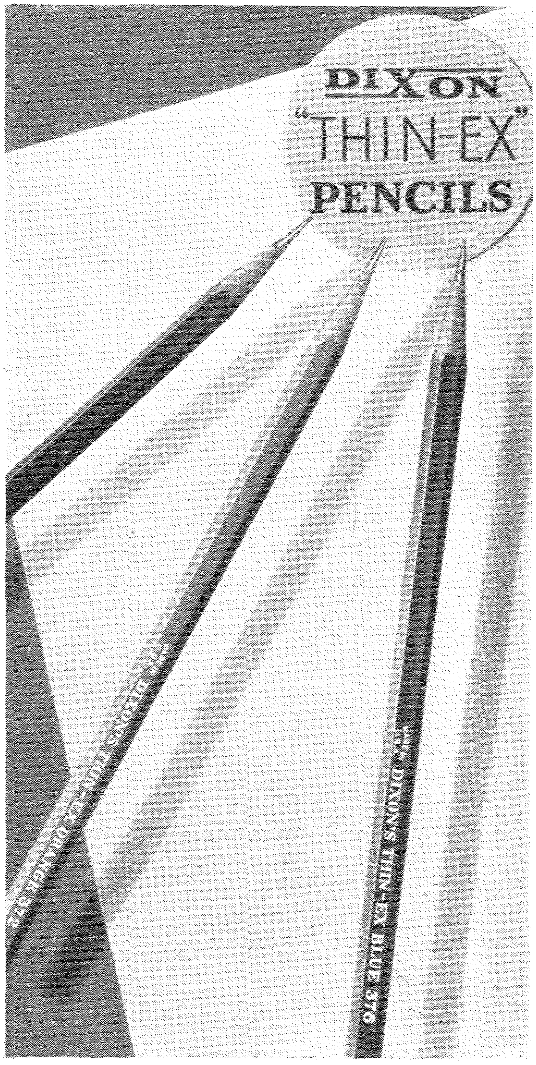

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Accountant, certified (N. J.) college graduate, 32, 5 years' commercial, 9 years' public experience having small clientele, seeks arrangement with accounting firm, Christian. Room 1214, Knickerbocker Building, New York City.

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Opportunity for acquiring a one-half interest in a public accounting practice in a thriving city, middle west, industrial section. Present practice is stable and with aggressive partner its present volume of $40,000.00–$50,000.00 gross fees can be doubled within very short time. Must be thoroughly competent, diversified experience, recognized qualifications and credentials and agreeable personality. Box No. 39, care of The Journal of Accountancy.

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