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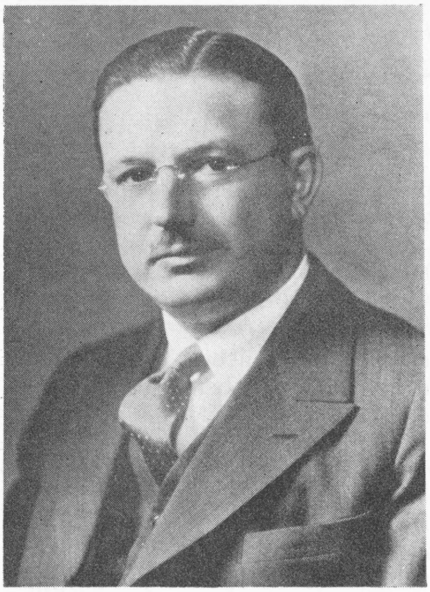

Mervyn B. Walsh has been engaged in the practice of accountancy for more than thirty years. He is a partner in the firm of Walsh & Company, Certified Public Accountants, Detroit.

In 1922, he founded the Walsh Institute of Accountancy, Detroit, a professional school.

From 1924 to 1926, Mr. Walsh was president of the Detroit chapter of the National Association of Cost Accountants and served as a national director of that association from 1931 to 1938.

For the year 1925-26 he was president of the Michigan Association of C.P.A.'s.

He is a member of the American Institute of Accountants; National Association of Cost Accountants; American Accounting Association; Michigan Association of C.P.A.'s; and Detroit Economic Club.

In this article Mr. Walsh discusses some postwar accounting situations, and presents his solution of the much-discussed problem of fully-amortized facilities which are still in use.

POSTWAR ACCOUNTING PROBLEMS

By Mervyn B. Walsh, C. P. A.

Accounting has its reconversion problems in common with industry and the same holds true for other professions. The multitudinous legislation passed in recent years has given an entirely new complexion to professional practice. The whole business structure has been affected and the attitude of executives changed.

War operations for most businesses resulted either directly or indirectly in one customer, with favorable prices and high profits. The fact that profits were subject to high rates of taxes and renegotiation contributed to general operating inefficiency. Expense controls were forgotten and the expression "the Government pays" became hackneyed. Unfortunately, many of these practices have carried over to present day operations.

With the resumption of competitive conditions it is mandatory that business revert to efficient management and detailed analysis of financial operations. Time was when financial statements were closely scrutinized with a view of expense control. Out-of-line items were carefully analyzed and eliminated when possible. Competition will be keen with increased productive capacity and there are many examples to date of one industry invading the fields of another. As production increases, intensive selling will begin and accounting for purposes of control will come to front. Evidence of this trend is present as you interpret comments of corporate executives, in their messages to stockholders.

Almost any cost accounting executive will relate the difficulties of cost control because of current labor conditions. Cost standards have lost much of their significance and cost variables have increased sufficiently to cause the establishment of new standards. With price regulation covering so many articles, and many articles being sold at a loss, accounting information must, of necessity, be placed in a primary position by management.

Notwithstanding the sociological problems of the day, the fact remains that commercial companies are organized primarily to earn a profit. The accountant has a clear-cut duty to produce from the financial books, operating statements that reflect any shortcomings, and to offer constructive suggestions that will act as a control on operating costs. As a result of war work, overhead charges have increased tremendously and the necessity of close pruning of many expense items is manifest.

There is no question that we are in an era where prices and expenses will be on a new level to keep abreast of economic conditions. Unfortunately the expense level has raised itself far above the price level in many cases. Clearly this is an opportunity for accountants to use technical skill to cause the price and expense levels to be in similar relation as in prewar times. The search for additional revenue has resulted in numerous new products to be fabricated. This condition calls for equitable treatment as between the old and new. Penalizing old products and favoring the new is a favorite pastime which should be frowned upon. Obviously the determination and proper use of costs will play an important part in postwar operations.

The metamorphosis that has taken place in accounting records has not received proper recognition in some companies. Account classifications are in use that are as antiquated as the Dinosauria. As a chart of accounts serves as a foundation for a proper accounting system and improved accounting procedures, thought may be given to this phase of accounting. To meet the exacting requirements of management, investors, and the public in general, new types of financial statements may well be adopted, that will be more informative in content.

War expansion is recorded in books of account in different ways, and the differences follow through to financial statements, often to be misleading to the reader. If plant capacity is in excess of present requirements, account classifications should be arranged to reflect the true conditions. Additional buildings and equipment acquired during the war period may have been covered by certificates of necessity and fully amortized at this time. Regardless of the fact that these assets have no book value and possibly no utility value, they continue to contribute to overhead expenses in the form of taxes, insurance, and the like. On the other hand, if these assets with no book value are making definite contributions to income without adequate charges to equalize normal depreciation the financial statements may again be misleading.

Journal entries to explain equalization of depreciation charges for cost and income purposes follow:

Appraised Value—Amortized
  Emergency Facilities $300,000
  Appraisal Surplus (Capital) 300,000

To establish current value of emergency facilities fully amortized.

Depreciation—Amortized
  Emergency Facilities ... $60,000
  Reserve for Depreciation—
  Amortized Emergency Faciilties 60,000
  For annual depreciation charges.
  Note— (Assuming a life of 5 years).

Manifestly the above depreciation charges must be restored to income for income tax purposes. By the same token the $60,000 depreciation charges may properly be transferred from Capital Surplus to Earned Surplus to reflect the true conditions. At the end of the five years the following entry will eliminate the emergency facilities from the books:

Reserve for Depreciation—Amortized
  Emergency facilities $300,000
  Appraised Value—
  Amortized Emergency Facilities 300,000
  To write off emergency facilties fully depreciated.

Conditions with respect to each company will vary and it is the accountant's function to provide procedures to meet requirements.

These illustrations make clear the need for changes in account classifications.

Moreover there are other changes without end that may be made to improve accounting records in order to keep management informed of current operating conditions. Labor and salary rates at increased levels call for consideration in charging these amounts to accounts. Overtime and other premium payments should be distinguished from normal payments to be measured against results obtained. For companies affected by war operations it is a fallacy to compare current operations with operations of war years. Comparisons of this nature are a direct violation of the principle that like things should be compared. Far better that comparisons be made with prewar years in order that increases and decreases carry their full significance. By the same token statements of financial condition may well be compared with statements reflecting condition prior to the war.

With market values exceeding book values by a large margin, there will be a temptation on the part of some to write up values to more nearly represent values in terms of market. Research will show that there was a distinct trend along these lines in the twenties and that capital assets were adjusted to reflect market values of those days. With changed economic conditions in the early thirties the trend reversed itself and there were all kinds of gymnastics on the part of management to write down capital assets to the much reduced current values. History repeats and it might be expedient to make a thorough study of cost versus market as applied to capital assets. To be able to discuss this topic fluently will be the task of accountants in the not distant future.

FEDERAL TAXES

In any discussion of postwar accounting questions it would be amiss to omit reference to Federal taxes. Taxes have such strange effects on business operation that some of the outstanding features demand mention. The first quarter of 1946 revealed widely divergent results in reporting income. Large losses were reported by a considerable number of companies, while other companies reported large increases in net income. The automotive industry was affected by strikes not only of producers but of suppliers as well. General Motors, Chrysler, and Packard reported as follows:

to grow, and nourishment for the corporation during the development stage is required. On this premise, profits are permitted to remain in the corporation for future expansion. If these profits should be in liquid form, difficulty is experienced in convincing agents that Section 102 of the Revenue Act is not being violated. If profits are distributed, no cushion may be available for loss years. Management is face to face with questions calling for unlimited business acumen correlated with rules of taxation.

To summarize, accountants must move into new thought fields in this reconversion era, and be qualified to discuss not only the items referred to herein but also supplemental questions by the score. Management expects and should receive the utmost in advice from accountants.

	General Motors	*Chrysler*	*Packard*
Operating loss	$88,988,663	$8,382,072	$3,465,449
Carry-back refund	52,864,000	7,150,000	3,218,000
Net loss	$36,124,663	$1,232,072	$ 247,449

While carry-back refunds are estimated, they reveal something new in taxation, when three companies reduce operating losses by more than sixty millions for three months' operation. The carry-back and carry-forward principle of taxation is bound to play an important part in financial forecasts.

For the smaller corporations, particularly those that are closely owned, taxation offers a confusing problem in the matter of officers' salaries. There is a wide hiatus in what officers feel they are entitled to receive in salaries and what revenue agents consider adequate. As the courts hold that each case is individual and depends upon facts alone for solution, the problem becomes more confusing. Officers' salaries stand out as a target for additional taxation and the wisdom of Solomon is necessary to find the line of demarcation that satisfies both the taxpayer and the Treasury Department.

Another matter in the field of taxation that remains confusing to the smaller corporation is the proper distribution of profits. Small businesses are usually anxious

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