1-13-1938

To the Presidents of Corporations Having Securities Listed on the New York Stock Exchange

John Haskell

New York Staock Exchange. Committee on Stock List

NEW YORK STOCK EXCHANGE

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January 14, 1938

To the Presidents of Corporations
Having Securities Listed on the
New York Stock Exchange:

As a result of the fall in commodity prices during the last few months, the Exchange has received requests for advice regarding the treatment in accounting statements of inventory losses and of differences between the present prices and the cost of goods contracted for but not yet received. The Committee on Stock List has given consideration to the question and has caused studies to be made to provide information upon which suggestions may be based, and has obtained advice on the accounting features involved from the Committee on Cooperation with Stock Exchanges of the American Institute of Accountants.

Treating, first, the question of annual reports as distinguished from interim reports, we feel that the following practices would be desirable:

(1) That each corporation should clearly advise its stockholders whether, as an incident to the conduct of its business, the corporation does or may enter into future commitments for the purchase and sale of commodities (such as rubber, cotton, wool, sugar, wheat, etc.) to such an extent that the amount of its commitments outstanding is or may at any time become a material fact in the corporation's position.

If stockholders have not already been informed as thus suggested, the information should be given in the next annual report.

If, after having once made a statement on this subject, there should be a change of practice, that fact should be indicated in the annual report next following such change.

(2)(a) If, at the end of any fiscal year, purchase commitment prices exceed current purchase prices to a material extent (assuming that a free market for similar commodities can fairly be said to exist), the corporation should disclose what is the approximate amount of the indicated excess of prospective cost of commodities at commitment prices over the value at market prices, and what amount of reserve has been provided or is available at the close of the fiscal year in respect of such difference. If and to the extent that purchase commitments are offset by firm sales commitments to responsible buyers, no reserve would be necessary, but it would be desirable that this fact should be disclosed.

If prices have fallen, but there is no free market for commodities similar to those covered by commitments, the circumstances should be sufficiently described in the report to make the situation readily understandable to stockholders.

(b) The procedure above outlined (which is analogous to that of valuing inventories at cost or market whichever is lower) is, the committee believes, in accordance with accepted accounting practice.

(3) The Committee recognizes and draws attention to the fact that the existence of commitments in large volume may, in a time of widely fluctuating prices, be a fact of material importance in the financial position of a corporation, even though at the date of the balance sheet market prices may be equal to or greater than commitment prices. It feels, however, that information on this point is not within the scope of the balance sheet or the accounts relative thereto, and that the question whether it should be given, and if so, how, forms a part of the general problem of supplementing annual accounts with other information bearing upon the position or prospects of the corporation, which

must be dealt with by corporate executives in accordance with the circumstances of the particular case.

The foregoing has to do primarily with annual reports. It is equally important to stockholders to be advised of the existence of any of the situations herein treated upon the occasion of an interim report. There are, however, three essential differences between interim and annual statements, namely, that the former cover only a fraction of a year, they are less complete, and they are usually unaudited. The Committee on Stock List has frequently pointed out that while it believes quarterly statements to be valuable to investors, there is an ever present danger that undue importance will be attached to them and unwarranted inferences drawn from them. In many cases losses which would be indicated under the foregoing treatments may be so large in proportion to the profit of a short period such as a quarter, that a statement which provided for the loss without indication of that fact, or of the amount of loss provided for, might be as misleading as one which ignored the loss entirely. The quarterly reports should at least show, in the event of the existence of any of the conditions herein treated, whether such conditions have been dealt with, and if so, in what way.

In all of the cases herein treated, whether in annual or in interim reports, executives should determine the precise form of presentation in the light of the facts of the situations of their respective companies, bearing in mind that the object to be sought is the enlightenment of both present and potential stockholders.

Yours very truly,

COMMITTEE ON STOCK LIST,

John Haskell

Executive Secretary.