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Valuation of Stocks for Excess Profits Duty

Great Britain

Valuation of Stocks for Excess Profits Duty

As this issue of THE JOURNAL OF ACCOUNTANCY goes to press important and most timely proposals as to valuation of stocks for purposes of the British excess profits duty are received. It is impossible to give more than the proposals themselves at this time, but in the October issue we hope to present the opinion prepared by firms of accountants in Great Britain and possibly some comment upon the significant modifications proposed. This matter deserves the earnest consideration of legislators and government officers in this country.

HEADS OF BRITISH GOVERNMENT PROPOSALS UPON THE VALUATION OF STOCKS FOR PURPOSES OF EXCESS PROFITS DUTY.

The government are prepared to adopt the following modifications—which will not require legislation—of the general principle that stocks should be valued at cost price or market value, whichever is the lower.*

* In considering this matter the government have had before them an opinion which has been expressed by members of certain eminent firms of chartered accountants. It will be seen that the govrnment proposals, whilst coinciding in the main with this opinion, depart from it only in the direction of more favorable treatment for the taxpayer.

1. A period will be allowed after the termination of the war in which to ascertain by actual realization the value of the stock appearing in the account at the end of the last accounting period, and an allowance made from the profits of that period or any difference between the valuation and the sum realized. The period proposed is a fixed period of a year from the termination of the war, for all businesses.

The loss (if any) on only such stocks as were in hand at the end of the last accounting period will be brought into the adjustment, but the whole of such stocks, not individual parcels selected by the taxpayer, must be considered.

The necessary sanction for this modification of general principles will be given by a regulation under section forty subsection three of the finance (No. 2) act, 1915.

2. Certain classes of industry require to keep stocks of raw or semi-manufactured goods for the purposes of manufacturing processes, and these goods are frequently of such an imperishable character that a minimum quantity required for a business could be held untouched for a long period.

Accordingly in any class of trade—

(a) which requires for its manufacturing processes to keep such stocks, and

(b) in which a recognized practice has obtained of taking a constant quantity at a constant price, the government are prepared to accept the practice. The government would regard goods as imperishable which are of sufficient durability to last without material deterioration during a period equal to the length of the war.

Any individual member of the class who has not adopted the method in his business may be allowed to do so for the purposes of excess profits duty, but may not claim as the constant quantity of stock so valued a greater quantity than the minimum amount held at any stocktaking in the three pre-war trade years.

Where a claim is made that an industry should be brought within this concession, the board of inland revenue will be prepared to receive representations and to consider evidence as to the existence of a material body of such practice in the industry and as to the character of the stocks to which it is claimed the method should be applied, with a view to securing the uniform treatment of all members of the industry.

The balance of stock above the minimum quantity in cases falling under this modification of the general principle is to be treated as in (1).

3. Profits derived from sales which reduce stock below the particular minimum or constant quantity adopted for any business are not the less trading profits. Where, however, a raw material is associated with plant in a manufacturing process (e.g., metal kept to a constant level in galvanizing baths), the board of inland revenue will consider claim under section 40 (3) of the finance (No. 2) act, 1915, that it is akin to a capital asset, like plant, which has been exceptionally depreciated (by depletion) or of which the renewal has been postponed.

4. Where in an industry or as respects a class of stock to which the foregoing (2) does not apply, the owner of a business has taken a quantity of stock at a base price, the stock will fall to be valued during the periods of liability at cost or market value, whichever is the lower, but from the final valuation (on that basis) there will be allowed a deduction of a sum (in pounds sterling) equal to the original difference (at the end of the standard period) between the valuation on the base method and a valuation on the cost or market value method. Alternatively the first stock valuation may be revised and put upon the general basis of cost or market value when the modification outlined in (1) will apply.

Correspondence

Cost Records and Profits

Editor, The Journal of Accountancy:

SIR: A recent editorial in the *Saturday Evening Post,* closed with the following statement: "We should say the first step in preparing for after-the-war conditions would be for every American manufacturer and merchant, no matter how big or how little, to instal a really adequate cost-accounting system—if he has not one already—and study it carefully, in order to detect his pile of deadwood."

The wisdom of this conclusion is unquestioned; but the manner in which it can be convincingly presented to those who would profit most by the adoption of correct cost-methods is difficult. The federal trade commission is probably doing more effective work in pointing out the need for better business methods than any other single agency now at work; and its helpfulness in matters of this kind is becoming generally recognized.

Cost-accounting is a term that is used in a restrictive sense, to refer to factory or production costs; and this is the sense in which it is, undoubtedly, most frequently used. In this letter, however, the term is used in its broader sense to apply to all expenditures in connection with a business.