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The Integration of Income and Surplus Statements

BY A. C. LITTLETON

FOR some years a change has been taking place in the form and content of the income statement. In an increasing number of published corporation reports, income and surplus are being combined into a single statement. This is a trend that ought to be extended for the reasons to be outlined below, and the possibilities for improving the statement's details ought to be explored while the development is still in the formative stages.

It was recognized some time ago that general surplus was becoming so mixed in content as to be no longer identified with undivided realized profits. This condition had the effect of precipitating a controversy as to whether surplus should be subdivided or regarded as an indivisible "excess" of assets over liabilities and capital stock. That controversy has now been settled, I think; both the Institute's "definition of earned surplus" and various changes in the corporation laws of a number of states have contributed to the present well defined practice of separately stating appraisal surplus, paid-in surplus, and earned surplus in the financial reports. But other controversial questions remain.

The Institute's definitions imply that the source of current cash dividends, as distinguished from liquidating and stock dividends, is earned surplus; the newer corporation statutes imply that the source may be either earned surplus or paid-in surplus, although a few states limit cash dividends from paid-in surplus to those declared on preferred stock. But neither the Institute's committee nor the state statutes have given a clear indication of other transactions that may properly be debited to the various surplus accounts. Obviously the measurement of the amount of assets that may be withdrawn by action of the directors is open to a great deal of confusion so long as debiting and crediting these accounts is not subject to some standard.

It seems inappropriate for details of accounting procedure to be enacted into statutes, and it will take a long time for all of the newer issues to be settled by court interpretations of existing corporation statutes. Under these conditions a clear duty devolves upon accountants to exercise leadership in resolving the issues in a satisfactory manner. Certain steps have been taken in this direction which ought to be reviewed before others which need consideration are mentioned.

One of these is the extensive use that has been made of a surplus statement when classification of surplus alone seemed to produce an inadequate disclosure. This, in many instances, was a distinct improvement, since the number and variety of adjustments to surplus were often such that the net change in the surplus balance in consecutive balance-sheets could not possibly convey the necessary information. But a surplus statement may not be entirely satisfactory. It may combine in one statement such diverse elements as adjustments to appraisal surplus, to paid-in surplus, and to earned surplus; and, even if limited to earned surplus, it may become a conglomerate of capital gains and losses, corrections of past-income calculations, equity remnants, accumulated undivided profits of the past, current net income, reserve appropriations and releases, and dividend declarations.

Another step in the direction of clarifying practices touching net worth was

the statement by an Institute committee of certain broad principles including the following:

1. Unrealized profit should not be credited to income account of the corporation either directly, or indirectly through the medium of charging against unrealized profits amounts which ordinarily fall to be charged against income accounts.
2. Capital surplus, however created, should not be used to relieve the income account of the current or future years of charges which would otherwise fall to be charged thereagainst.

Clearly these sentences are intended to offer guidance, so far as broad statements can, to the proper treatment of certain types of transactions which may seem open to disposition in one of a variety of optional ways. The point is that some charges that have been made to capital surplus are of doubtful propriety. Even if there were no statutory prescriptions to this effect, appraisal surplus and paid-in surplus should not receive charges or credits which ought to be made in current income or earned surplus.

Both of these actions, one a growth of practice, the other carefully considered opinions of an Institute committee, deal with a possible confusion of thought regarding the treatment of certain transactions affecting net worth. These progressive steps ought to be followed by others that will still further clarify practice.

The integration of income and earned surplus into one statement is one of these further steps; a statement of the implications of the two broad principles given above is another. Some suggestions are here offered on the latter point, the remainder of the article being given over to the first.

Accountants might well agree that certain typical items should be charged against capital surplus, the implication being that items not mentioned should be associated with current income or earned surplus. An opinion of this sort, if authoritatively supported, would reflect the treatment that accountants felt was proper in view of the purposes and uses of accounting reports, even though some other treatment might be permissible under the statutes of a given state.

Debits to *revaluation surplus* are acceptable for the following:

1. Transfers to stated capital for stock dividends.
2. Fixed assets previously written up, now written down (not to exceed the amount of the original write-up credited to revaluation surplus).
3. Intangibles originally brought into the accounts by a credit to revaluation surplus, now written off.

Debits to *paid-in surplus* are acceptable for the following:

1. Transfers to stated capital for stock dividends.
2. Transfers to stated capital to raise low par to a higher par.
3. Intangibles originally brought into the accounts through security issues, now written off. (If necessary, create paid-in surplus by a reduction of stated capital.)
4. Loss from sale of reacquired shares or from retirement of reacquired shares purchased at a price above stated capital per share. (*Query:* Should this last debit be limited to the prorata portion of paid-in surplus applicable to these shares and the excess charged to earned surplus as a distribution of profits?)
5. Deficit from earned surplus account after including the operating results of the current period. (If necessary, create paid-in surplus by a reduction of stated capital.)
6. Cash dividends (other than clearly liquidating distributions) only when specifically permitted by the controlling state statute and then only for the purpose of protecting the continuity of preferred dividends during a temporary failure of current income to cover.

Although the above may be an inadequate consideration of the treatment of capital surplus, it is here assumed to be sufficient to establish the point that items which properly affect appraisal surplus or paid-in surplus have no place in a statement of earned surplus, whether the latter is reported separately or in association with the income account. Having thus limited the transactions involved, I can now turn to the subject proper—the integrated income-and-earned-surplus statement. After analyzing the essential purpose of financial statements in order to develop the theory which supports the integrated statement, and outlining the arguments for and against its use, I will consider the form and content of a satisfactory statement of this kind.

The general purpose of financial statements is to serve as a medium by which those in active charge of the affairs of an enterprise report important factual information to absentee interests.

As usually explained, the balance-sheet conveys information regarding (1) the relation of various equities to each other, and (2) the relation of the equities to the assets which support them; and the income statement conveys information regarding (1) the corporation's earning power as indicated by recurring transactions, and (2) the total results of the efforts of management to employ the capital of the enterprise in an effective manner. Thus each statement serves in a dual capacity; and the full purpose of each statement is achieved only if the form and content reflect both aspects.

The usual explanations of the nature of financial statements are more appropriate to simpler situations wherein the correlation of the two is clear than to modern situations wherein numerous complexities make difficult a suitable correlation of the two principal statements. For this reason it may be helpful to re-examine the objectives of the income statement, especially in regard to the question of whether under modern conditions the statement can still serve at the same time as a report of earning power and a report of managerial effort.

If we clear our minds, for the moment, of traditional forms, we can recognize as significant the fact that it is assets which constitute the focus of interest for management within the corporation and for all classes of investors without. Other data are supplementary. It is assets that are invested by stockholders and creditors; assets are the means of operating the enterprise and the means of discharging its obligations; an increase in assets is the objective of enterprise activities and the hope of investors. In a very real sense, businessmen are "asset-minded," and accounting can be considered as definitely oriented to assets and their various ramifications.

If one were to attack *de novo* the problem of corporate reporting, it might seem sufficient, in view of this central interest in assets, to report only the assets held now and those held a year ago. Much could be learned from such figures: the changes in each kind of asset would be clearly evident, and the increase (or decrease) in the total could be readily calculated. These would be significant facts. If the total were wisely distributed among different kinds of assets, having in view the nature of the enterprise, and if the total showed a reasonable increase, in view of the then current business conditions, there would be clear grounds for satisfaction.

Some people might be content with such reporting; but others of a more inquiring turn of mind would wonder which of the changes that were so readable in the comparative asset table were due to additional investments or withdrawals by stockholders and creditors, which to appraisal write-up or write-down, and which to the active administration of the assets in the midst of current business conditions.

Assets and the changes therein are indeed the central interest of all concerned, but a reporting of assets alone would be quite inadequate to the user's need, because the results of various differing causes would be indistinguishable.

Each asset, in spite of careful classification by type, arises out of a variety of antecedents. The person with an inquiring turn of mind will want supplementary figures which will help him to isolate and judge the different kinds of asset changes. He will wish to view the assets in the light of the diverse interests of the various parties who have contractual rights in them, and he will like to have the means of viewing the assets in a manner designed to give him some insight into the effectiveness with which the assets have been acquired, manipulated, and exchanged under the direction of management.

If one has a certain ingenuity with figures, it would not be difficult, granting reasonably complete records of transactions, to supply informal supplementary details which would very effectively illuminate the asset table. One of these supplementary tables would consist of a list of the present equity accounts and those of a year earlier (obviously the items on the right side of ordinary balance-sheets). A comparison of these equity figures would reveal: (1) the (net) change in assets due to investments and withdrawals by creditors and stockholders, or to appraisal revaluations, and (2) significant alterations in the elements of the equity structure and changes in the relation of various equity items to the total. Another supplementary analysis would explain all other asset changes. This one would set in contrast, (1) a report of efforts (expressed in costs, expenses, and losses) made in the expectation of inducing a net inflow of new assets, and (2) a report of the accomplishments (expressed in gains, incomes, and revenues) achieved by managerial activities in the setting of current business conditions.

This is but another way of saying:

Assets and their ramifications constitute the central interest of all parties concerned in a corporation.

The equities sides of two balance-sheets are in effect supplementary analyses which by comparison will reveal those asset changes which are involved in the administration of equities.

The income statement is, or should be, a supplementary analysis of the remaining asset changes—those involved in the management's efforts to use the assets effectively.

By the tradition of double-entry bookkeeping the balance-sheet is given primary place and the income statement is considered as a subordinate analysis of the noninvestment changes in proprietorship. But the essence of the theory of financial statements is, I think, better outlined if the reports are explained as above in terms of assets and asset changes. It then becomes evident that: (1) balance-sheets alone are inadequate reports, (2) assets are a jumble of items derived from a mixture of equity transactions and economic transactions, and (3) the recent emphasis on the income statement is a natural result of perceiving the fact that herein lies the clue to enterprise value and managerial efficiency.

Such an explanation does not of itself bring about any alteration in the form of the usual statement. But it does show that under some conditions the content of the income statement may be something less than the theory of financial statements indicates that it ought to be.

The income statement is not in accord with the theory of financial statements:

1. When it includes elements which are related to capital surplus in any of its forms.
2. When it includes some of the results of equity transactions that are entered upon for their financial effects

but produce net balances which have a surface similarity, as debits or credits, to losses and gains.

3. When it neglects to reflect all transactions in asset utilization (those entered upon for their productive effect).
4. When it reflects an overemphasis upon recurring earnings to the exclusion of nonrecurring losses and gains.
5. When no provision is made for including corrections of prior calculations of net profit.

When the reverse of these propositions is true, the income statement will be more nearly in harmony with financial-statement theory. It is brought in closer accord whenever capital-surplus adjustments are excluded from earned surplus and whenever income and earned surplus are integrated into a single report. Some progress is being made in this direction. But more progress would result, I think, if the reasons for and against an integrated statement were carefully weighed.

An important reason in favor of the use of an integrated income-and-earned-surplus statement is that this arrangement will tend to highlight the estimate character of periodical financial reports. This emphasis is needed because too many people regard the final figure of the income statement as a fully established, indisputable fact. The truth is that the only complete measurement of enterprise profit or loss would be one obtained by considering the concern's life history from inception to termination as a unit. Obviously no one with an interest in the business can wait so long for useful information. The next best thing is for the interested parties to receive a series of periodic reports of profit and loss, the summation of which will approximate this over-all result as closely as may be. For the periodic statements to be of this order, it is necessary for them to include all items of income and expense, and profits and losses of every kind.

Even though ledger accounts are periodically closed according to bookkeeping technique, the real nature of the asset increments and decrements which we call income and expense is that of a statistical series subject to correction when later information reveals the inaccuracies of sincerely presented past estimates. If the periodic net yields of business activities were recorded in purely statistical form, the figures could be easily adjusted to reflect the latest information, and the user would have before him revised figures from which he could alter his prior judgments. But no bookkeeping technique is available for making a "spread-back" of corrections into the accounts of the periods when the amounts would have been reported if foreknowledge could have been had. Accountants have not concerned themselves with purely statistical tabulations; and controllers could no doubt do so with advantage.

Since we cannot do without periodic reports in business and since purely statistical techniques are not suitable for accounting, an acceptable substitute is sought in a fully integrated income-and-earned-surplus statement. And in order to constitute a useful substitute this statement should be constructed in harmony with the theory of financial statements, especially with regard to the five points outlined above.

Against this view several arguments are advanced. Adjustments clearly labeled in the income statement as corrections, it is said, may be construed as unfavorable reflections upon well intentioned management, since errors in past estimates are unavoidable in any event. The answer is that only the correction of those errors which were conceivably avoidable by better foresight or different policies would be a reflection upon management; no one can reasonably expect management to be clairvoyant and infinitely wise.

It is also asserted that the inclusion of earned-surplus adjustments in the

income statement will destroy the comparability of successive periods and will distort the reporting of recurring earned income by associating nonrecurring and unusual items with it. The answer is that properly organized statements will still be as comparable in their details as present income statements are; in comparative statements nonrecurring items would not be expected to repeat in successive periods. As to "distortion," that is something which depends on the point of view. The doctrine of distortion of the final figure usually assumes smooth regularity to be the natural phenomenon. Yet there is just as much justification for considering irregularity of the final figure as normal, in which case "smoothed regularity" would be the distortion.

The doctrine also assumes, erroneously I think, that the final figure will be the only significant amount and that it will, because of its position alone, become the multiplier when a reader undertakes to capitalize net income as a test of enterprise value. I think that to take such a position is to underrate the intelligence of the user in interpreting the statement subhead "nonrecurring." More errors of judgment would probably rest upon neglect to note the significance of nonrecurring items than from possible inadvertent overemphasis in considering them.

"Distortion," as usually thought of, is no doubt an outgrowth of the processes of accruing and deferring. So much progress has been made in accruing expense before disbursement and in deferring costs after disbursement that this quasi-scientific refinement of accounting should be preserved and extended. Perhaps it is this thought that gives rise to the notion that incorporation of nonrecurring items within the structure of the income statement will negative all of the good work that has gone into the skilful building of accruals and deferments into accounting. I am not disturbed by that fear. Whenever regularity can be detected and the amounts measured by dependably objective methods, it should be recognized in accounting procedure, for the effect is that the remaining irregular occurrences will thus be revealed and isolated for study. The unattainable ideal is that all irregular occurrences will be eliminated through the complete perfection of the accrual system. But the fact that this is clearly unattainable should not be warrant either for excluding occurrences from the accrual system when dependable estimates can be made, or for extending the idea of the system so far that in some respects the effect is merely arbitrarily to smooth out irregularities that are inescapably irregular. Too many of the items often found as adjustments of surplus are objectionable on this very ground—their lump-sum disposition in surplus has the effect of leveling past, and perhaps future, calculations of earned income. Such items should by all means come to the eye of the reader as he examines the statement of earned income.

Another objection to the combined statement is that its use will lead to ignoring the distinction between capital losses and operating losses (and gains). The answer is that too much has been made of their distinctions—for they are distinct in some particulars—while their elements of similarity have been ignored. It is their likeness as similar aspects of asset changes which logically brings them into contact within the combined statement; their distinctions can still be revealed in the organization details of the statement. Thus nothing is lost and another advantage is gained.

It should perhaps be added that the more carefully one examines so-called capital gains and capital losses, the more evident it becomes that all losses and gains decrease or increase economic capital (assets) and are therefore equally entitled to be called "capital" losses or

gains. No doubt the terminology was intended to isolate liquidation and reorganization adjustments from those resulting from the usual course of business. But the argument and the procedure are both poorly adapted to the reporting of a going concern. It is difficult to see how a going concern can suffer liquidating losses (chargeable against stockholder investment) without cancellation of current profits, or how a going concern can, by mere resolution, reorganize its financial structure, absorb a large loss of assets, and still carry an earned surplus undisturbed.

There are several other arguments supporting an integrated statement. Surplus adjustments are accounting technicalities that are likely to be confusing at best to many readers. But their significance is more likely to be given consideration and understanding if they are definitely associated with current income figures than if they are separately reported. This is true whether the statements are conceived as a service to the "man on the street" or to skilled investment analysts and advisers. The use of the integrated statement should help the former to avoid the erroneous conclusion that recurring income is the only element that matters, as he would tend to do if the last figure in the statement were derived before surplus adjustments. It would also be appreciated—as a convenience, if nothing else—by the latter group, for those individuals seek the quickest approach to the best evidence of managerial foresight and decisions.

The counterargument is not very strong. It is that one technical arrangement will be no more useful to the uninformed than another; that a separate surplus statement gives all needed information and thus is an adequate disclosure to the informed reader; and that the latter's purpose is served if the surplus statement is placed near the income statement without being integrated with it. The answer is that these things may be true, in a measure, if adjustments of capital surplus have been excluded and if "integration" is considered to consist merely of attaching the surplus statement, by running additions and subtractions, to the end of the income statement. But I believe that a better articulation of the two statements, as later discussed, will prove more useful to even the best informed reader than either a separate or a loosely attached surplus statement. If this is true, the above argument falls.

The practice of relating income and earned surplus is clearly evident in published reports. A sample was examined consisting of thirty reports of 1937 and 1938 wherein some form of combined statement was used. In a few instances some such combination had been in use in 1912 or earlier; a few other companies began the practice between 1918 and 1924; nine of the companies made such reports as early as 1925 to 1929, and ten began the practice between 1930 and 1937. A more extensive examination of a large number of reports for industrial corporations as of 1938 showed that 28 per cent used an articulated statement running from sales to earned surplus; 28 per cent reported income and surplus separately but on the same page; 35 per cent reported the two on opposite pages; and only 9 per cent omitted earned surplus adjustments entirely or reported them otherwise than indicated above.

The simplest arrangement (using here only the lower part of the statement) was as follows:

Net income..................	000
Earned surplus, beginning of year	000
	000
Dividends..................	00
Earned surplus, end of year.....	000

Another typical arrangement was:

Net income for the year.........	000
Surplus at beginning of year.....	000

Surplus before adjustments and dividends	000
Surplus adjustments, charges (detailed)	000
Surplus adjustments, credits (detailed)	000
Surplus before dividends	000
Dividends: on preferred	00
on common	00
Surplus at end of year	000

Another type of data organization occasionally met produces a "clean" surplus:

Net income from operations for the year	000
Add: (Various adjustments, itemized)	00
	000
Deduct: (Various adjustments, itemized)	000
Net profit added to surplus	000
Surplus, beginning of year	000
	000
Deduct, dividends (detailed)	00
Surplus, end of year, per balance-sheet	000

The issue present in these developments of practice is one of the degree of intimacy with which the statements should be articulated in order to conform closely to statement theory. There are several gradations:

1. No articulation: Earned surplus adjustments are not reported or are separated spatially from the income statement.
2. No articulation: The statements are separate but surplus is presented close to income.
3. Simple articulation: Earned surplus statement, including adjustments, is attached to income statement by running additions and subtractions.
4. Complete articulation: "Clean" surplus is attached but adjustments are integrated with operations above "net profit added to surplus."

In my opinion, complete articulation is the most desirable arrangement because (a) it makes the statement a close reflection of statement theory as outlined above, and (b) it discloses the significant interrelation of the items by which management reports upon its utilization of the assets—that is, operating transactions and earned-surplus adjustments.

If this reasoning is accepted, the problem then becomes one of examining the meaning of "complete articulation" and "integration of operations and earned-surplus adjustments." The rest of the discussion is given over to this problem.

There are two principal parties who are interested in the income statement: management and investors. Management needs a classification of data in the statement that will distinguish operating and nonoperating items as an index to efficiency; investors need a classification of data that will distinguish nonrecurring and recurring items as a basis for judging (a) immediate dividend possibilities, and (b) earning power as an element in estimating enterprise value. To satisfy these needs, the statement will fall naturally into two major divisions:

1. Recurring: operating.
   nonoperating.
2. Nonrecurring: operating.
   nonoperating.

These divisions will need suitable subsections in order to derive significant sectional and accumulated results.

1. Recurring transactions for the year.
   a. Recurring operating income.
   b. Recurring operating expense.
   c. (Sectional result)—Operating net income.
   d. Recurring nonoperating income.

   e. Recurring nonoperating expense.
   f. (Cumulative result)—Recurring net income.
2. Corrections of recurring income and expense of prior years.
   a. Charges.
   b. Credits.
   c. (Cumulative result)—Recurring net income as adjusted.
3. Nonrecurring transactions.
   a. Realized losses.
   b. Unrealized losses.
   c. Realized gains.
   d. (Unrealized gains?)
   e. (Sectional result)—Net nonrecurring losses (gains).
   f. (Cumulative result)—Net yield for the year added to earned surplus.
4. Earned surplus.
   a. As of beginning of year.
   b. Changes in surplus reserves.
   c. Dividends.
   d. As of end of year, per balance-sheet.

This arrangement classifies the data into sections primarily according to the interest of investors and investment analysts, and gives operating and nonoperating items for the use of management a somewhat subordinate place because management has more facilities than the investor for making supplementary calculations.

The terminology for the subtotals is selected to point to a distinction between "operating net income," "recurring net income for the year," and "net yield for the year"; and the titles of the sections frankly abandon vague and undescriptive terms such as "other charges" and "other credits."

Comparability is important and significant down through "recurring net income," since these are data indicative of earning power. Beyond this point the data are not significant in comparison with similar sections for prior years. In the "corrections section" sufficient information can be given (approximate years involved being stated in parenthesis) to enable analysts, if they care to do so, to "spread back" the corrections over past periods as a statistical adjustment to their own tables of reported net income of prior years. In the "nonrecurring section" management reports to investors upon the results of various managerial decisions which have affected the final showing of profit or loss without directly influencing the day-by-day flow of regular activities.

The above tabulation gives only the framework of the kind of statement here tentatively suggested; the details with which the sections would be filled in would vary with the circumstances of the particular fiscal period and the peculiarities of different kinds of business. But it is also probable that the assignment of details to sections would tend to vary somewhat with the interpretation placed on a given transaction or situation by the accountant concerned. Here is a fertile field for research and study. A great deal of thought ought to be given to a variety of specific situations and the place in which they should be reported.

To produce examples of the need for debate on the reporting of particular items, a special study was made of the thirty statements of 1937 and 1938 previously mentioned, and about fifty items were selected from the reports to represent situations which might conceivably be reported in different places in the integrated statement. Differences in the placing of similar items were evident in the published reports themselves, and a questionnaire addressed to members of the Institute's committee on accounting procedure revealed further differences of opinion in the replies received.

It is not proposed here to discuss the reasons for or against any particular location in the statement for these items; to do so would be difficult at best because the real nature of many items cannot be read out of their brief designation in the published reports. But a list-

ing of the items may be helpful in showing the existence of many aspects of statement formation that need examination in the interest, not of any prescribed uniformity of treatment, but of a clearer common understanding of the way skilful classification can contribute to good reporting.

The following items are stated substantially as worded in published reports. For purposes of study this question may be asked for every item: Where in the above outline of subsections of the tentative, integrated statement of income and earned surplus should this kind of item be reported?

There was a general agreement in the small sample studied concerning the location of the item, "Idle facilities expense."

Flood-prevention cost
Dry-hole losses
Losses on investments sold
Gains on redemption of investments
Premium on own bonds purchased and canceled
Recovery of receivables previously written off
Provision for pending litigation
Provision for foreign losses

A majority of the opinions obtained were in agreement regarding the location of the above items. The same was true for the next section of the list, but the preferred location was not the same as for the items above.

Provision for property abandonment
Losses from floods
Gains from sale of capital assets previously written down
Adjustment of contracts regarding operations of prior years

There was also substantial agreement in the small sample of opinion as to the location of the following items, but the preferred location was different from either of those chosen for the two sections of the list given above.

Provision for contingencies
Provision for development and extension
Return of appropriations not required
Previous charges to reserves now transferred
Return of prior provision for cumulative preferred dividends
Premium and discount on preferred stock redeemed
Excess of cost over stated value of preferred stock retired
Adjustment of low par to $100 par

The choices expressed for a number of items such as the following were so scattered that no preference was discernible in the small sample.

Provision for current federal taxes
Additional federal taxes for prior years
Provision for equalization of inventory prices
Property retirement not covered by depreciation reserves
Provision to reduce value of investments
Write-down of intangibles
Loss on capital assets
Loss on retiring bonds before maturity
Discount on own bonds redeemed and canceled
Net premium, discount, and expense on redeemed bonds and stocks
Charges for preferred-stock refinancing

Other choices were so nearly balanced between two alternative treatments as to be undecisive.

Return of excess of reserves for receivables of prior years
Loss on settlement of lawsuits (no prior reserve)
Loss on leases expired or forfeited
Gain on insurance recovered
Gain on sale of leaseholds and equipment
Gain on own bonds retired
Discount and premium on own bonds acquired for sinking funds
Reversal of prior capitalization of leasehold costs
Write-down of land values
Excess of balance-sheet value of subsidiary company purchased over cost in stock

Reduction of stated capital
Prior deficit absorbed by surplus from reduction of stated capital.

In conclusion, this brief study of the theory and practice of income-statement formation seems to lend emphasis to the thought that there is need for (1) a thorough examination of the possibilities of an integrated income-and-earned-surplus statement to assure the separation of adjustments to earned surplus and those to capital surplus, and (2) a re-examination of the sectioning of the statement in the interest of a more informative organization of the data.

The fundamental proposition is this: The content and organization of the major statement accompanying the balance-sheet should be such as to constitute an informative analysis of the efforts of management to employ the capital of the enterprise in an effective manner. If this is an acceptable statement of purpose, it follows that the earned-surplus-and-income statement must be combined in some way so that "management efforts" may be reported in one coherent statement for the study of investors.

The art of full and clear reporting admittedly presents many difficulties. But the alternative to facing and overcoming some of the difficulties is to leave in practice such a wide diversity of treatment for apparently similar items as to give the impression to some readers who compare corporation reports that corporations can treat various items about as they choose and still be within the range of someone's views of what are "accepted principles of accounting."