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Correspondence

M. E. Murphy

Edwin S. Reno

John Kunkel

E. S. Woolley

Henson, Gates & Company

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CORRESPONDENCE

Students' Societies

Editor, THE JOURNAL OF ACCOUNTANCY:

DEAR SIR: Any profession may enhance that *esprit de corps* among its members which is one of its most valuable, if least tangible, assets by providing opportunity for close association of its aspirants with each other and with some of its outstanding practitioners.

Accounting firms generally recognize that their juniors' educational background should keep pace with their enlarging professional experience, and that it is increasingly important to build up their general cultural and accounting backgrounds as well as their ethical standards in order that a unified approach may be made to accounting problems.

Little opportunity is afforded C.P.A. candidates to hear lectures given by leaders in the profession and in related fields. This is particularly true in areas devoid of local branches of state societies and universities. In the infancy of American accountancy, practitioners gladly gave their time for the organization and presentation of lectures for students, but as the profession has expanded formal educational activities have been delegated to universities, and preparation for C.P.A. examinations has reverted to correspondence and coaching schools. The Institute's committee on education has maintained a continuing interest in university accounting curricula, but the problem of the post-high-school and post-university education of accountants remains unsolved. The former of these two groups merits special attention as more than one-half of the examination candidates are drawn from it.

In the light of these facts, it is suggested that the Institute and each state society might well organize a student society within each state, draft its constitution, select from state society membership the students' society president, and provide it with a minimum reference library. The sponsoring organizations should arrange for an annual

series of lectures to be given to the society by accounting practitioners and professors, members of the bar, economists, and financial experts, as well as for discussions of the Institute's examinations and an annual dinner. The lectures, which should be of such high calibre that the best of them could be made available to the whole profession through the medium of *THE JOURNAL*, should not pertain solely to accounting and auditing procedures, but should include discussion of professional standards, ethics, and problems. They should be followed by general student discussion which would enhance the extemporaneous speaking abilities of the participants. Throughout the year the Institute's president and council members should visit the various students' societies to the end of maintaining a unified program for the development of young practitioners.

The students' societies would provide opportunity for social intercourse between their members and established accountants. Through this informal association, practitioners would expand their contact with the neophytes and would assume some responsibility for their training, and students would be stimulated by personal conversation with men who would otherwise be known to them only by reputation. The gulf between the older members of the profession and candidates for the Institute's examinations would tend to be less wide.

It is submitted that the Institute in coöperation with the state societies should make a survey of the activities of English students' societies, the history of which since 1883 presents many and varied aspects for consideration. Such a study would reveal, it is believed, the adaptability of the organization and methods of English societies to American conditions, and the expectation of the service similar American societies would render in developing well trained and progressive young accountants. Other outcomes of students' societies would be the increase of their members' interest and participation in a pro-

fessional organization, the furtherance of their knowledge of the profession's heritage, and the development of their individual distinction of manner and clarity of thought—indices of the learned profession of which, it is hoped, they will eventually become distinguished members.

Yours truly,
M. E. MURPHY

New York, N. Y.

The Valuation of Compensation Stock

Editor, THE JOURNAL OF ACCOUNTANCY:

DEAR SIR: I was very glad to find in the September, 1939, issue of THE JOURNAL the letter of Edwin S. Reno commenting on my article, "The Valuation of Compensation Stock," which appeared in the July, 1939, issue.

In the article, I expressed an opinion that any rise or fall in the market value of the compensation stock between the dates when the employment contract was made and the stock issued should be unrealized gain or loss of the employee at the latter date. I said "unrealized" because I did not intend that the employee should account for it (in his income-tax return) when he received the stock. I think he should account at that time only for the value of the stock at the date of the employment contract, and that this amount should become his cost basis upon actual disposition of the stock at any time.

The incentive provided in a stock-compensation arrangement lies primarily in the employee's opportunity to acquire a proprietary interest in his company, and this seems evident from the fact that employees are usually expected to retain their compensation stock, not sell it. An agreement not to sell such stock except under certain conditions is often written into the compensation contract.

Since fluctuations in the earnings of the company produce a much smaller reaction marketwise than general economic conditions, which no individual employee can influence to an important extent, and as fluctuations in the market price of the stock do not affect the earnings of the company (unless market price is used in valuing the stock charged to salary expense), it is not clear how the market price on the particular date when compensation stock is received by an employee can be a measure of the value of his services.

The fact that there are a number of court decisions on the question should be no bar to further discussion, particularly when the purpose is to bring out considerations which might lead to a more equitable and satisfactory conclusion.

The argument that market price on the date of receipt should be the basis of value, because that is the first time the employee

Estate Tax, Deduction for Charity

Editor, THE JOURNAL OF ACCOUNTANCY:

DEAR SIR: Reference is made to Greeley's excellent article on the above subject, the conclusion of which appeared in THE JOURNAL OF ACCOUNTANCY for July, 1938. In the case given and worked out by Mr. Greeley, there is an interdependency between (1) the deduction for remainder to charity and (2) the total New York and federal estate tax.

Mr. Greeley undoubtedly follows the best procedure in first computing tentative taxes, ignoring for the purpose of the tentative computation the effect of those taxes on the deduction for remainder to charity. This confines the subsequent calculations to the top-bracket rates.

From that point on, however, the computations can be somewhat simplified and the necessity of solving simultaneous equations in each case eliminated by proceeding along the following lines:

Tentative New York tax	\$35,623.28
Tentative federal tax	156,249.79
Total tentative New York and federal taxes	\$191,873.07

Combined effective top-bracket rates:

New York =	
.15631 × .662 × .07	= .0072434
Federal =	
.15631 × .6681 × .2301881	= .0240387
Combined	= .0312821
1 minus above	= .9687179
Correction factor =	
.0312821	= .03229227
.9687179	
Correction =	
\$191,873.07 × .03229227	= 6,196.02
Corrected, or final, total taxes	\$198,069.09

Note that:

.662 = 1 - .338
.6681 = 1 - .3319
.2301881 = .98371 × .234
where .98371 = 1 - .01629
and .234 = .29 - .06 × .07

Yours truly,

EDWIN S. RENO

Pittsburgh, Pa.

comes into possession of an asset which may either be sold or retained, seems inconsistent with the rule in the case of instalment subscriptions for stock, payable in money. An agreement to work out the consideration for the issue of shares seems to parallel closely an agreement to pay for the shares in money at a future date. In both cases the price on the date of the agreement should be the cost basis of the stock to the recipient. Value is always a matter of judgment, but it is more usual to exercise judgment as to value when the contract is made, even though transfer of legal title to the subject matter is to be made in the future.

Yours truly,

JOHN KUNKEL

New York, N. Y.

Apportioning Income on F.H.A. Loans

Editor, THE JOURNAL OF ACCOUNTANCY:

DEAR SIR: Reference is made to the question and answers on "Apportioning Income on F.H.A. Loans" appearing on page 52 of the January issue of THE JOURNAL OF ACCOUNTANCY.

The method outlined by the questioner is, in my opinion, more nearly accurate than those suggested in the answers. The reason for this opinion is that the services to be performed by the seller of this mortgage (that is, the questioner) will increase as time goes on. There will be more services per year and therefore more costs during the last five years of the contract than during the first five.

On the other hand, the cash received (which they are calling here "interest differential") will be considerably less during the last five years than during the first. If then all receipts are taken up as earned income during the early years they will be faced with considerable operating loss during the last. And the more mortgages they sell the worse that condition will be.

This "interest differential" is in reality a true service fee, even though it is based on the amount of the mortgage, the presumption being that the larger the property the more service (such as seeing that the building is maintained in good condition, etc.) will be received. Because of this I believe that it is correct to defer income during the early years and apportion to the costs of the later. The

straight-line basis suggested by the questioner has the advantage of simplicity.

Yours truly,

E. S. WOOLLEY

New York, N. Y.

Auditing Procedure in America

Editor, THE JOURNAL OF ACCOUNTANCY:

DEAR SIR: In your comments on the article on "Audit Procedure in America," published in *The Accountant*, you invited readers of your JOURNAL to express their opinions on the phases of accounting mentioned.

We thought that a few comments on the practice in Australia may be of interest.

As you know, accountancy in the British Empire is modeled on the English pattern. This is particularly so in Australia. However, of late years, American texts have been studied more and more by the progressive practitioners.

The matter of the inventory valuation verification is one of the most difficult for auditors. In the Kingston Cotton Mills case, it was said, "It is no part of an auditor's duty to take stock." However, this does not absolve the auditor from making any attempt to verify the stock valuation. In his work, *The Principles and Practice of Auditing*, which is one of the leading British textbooks on auditing, De Paula said, "An auditor today would be running considerable risks if he acted too literally upon this decision, which is an old one, and opinions and practice have changed greatly since this case was decided." The practice today is for the auditor to mention in his report, or in the balance-sheet, that the "stock is as per general manager's valuation," etc., but during the course of his audit he obtains the stock sheets and by the use of various checks and comparisons, and, if possible, by making test checks of quantities, the auditor can form some opinion as to the accuracy or otherwise of the valuation; and can act accordingly.

In Australia, circularization of the client's customers for the verification of trade accounts is customary. This firm uses a gummed slip which is affixed to the usual statements of account, checked and verified with the trade ledgers, and dispatched through the post by our employees. This is done about twice in each financial year.

The affairs of trading companies are gov-

Correspondence

erned by the companies acts of the Australian states. The New South Wales act provides:

1. That proper financial and corporate records shall be kept.
2. That an auditor shall be appointed and his remuneration fixed by the shareholders in general meeting each year.
3. That the auditor shall make a report to the shareholders, reporting:
 - a. Whether or not all required information and explanations have been obtained.
 - b. Whether in his opinion the balance-sheet referred to in the report is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs, according to the best of the information and explanations given to him and so shown by the books of the company.
 - c. Whether or not, in his opinion, the corporate records have been properly kept.
4. The auditor shall be entitled to attend any general meeting of shareholders, at which his report is laid before the company, and may make any statement or explanation he desires with respect to the accounts.

These provisions do help the auditor to carry out his duties and a general form of report has come into use. The following form is the general one used by this firm:

AUDITOR'S REPORT

We report to the shareholders of the Commercial Equipment and Service Company Limited that we have examined the financial records of the company for the financial year ended 30th June, 1939, and that, having obtained all the information and explanations required by us, we are of the opinion that the above balance-sheet is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs according to the best of our information and the explanations given to us and as shown by the financial records of the company. The corporate records have, in our opinion, been properly kept.

HENSON, GATES & Co.,
*Certified Public Accountants,
Auditors to the Company.*

In general, the profession in Australia welcomes any move that tends to make the profession of greater use and benefit, and is ready to cast off out-of-date practices. That auditors should pay more attention to principles and take cognizance of trends in public thought is, we believe, essential.

Yours truly,

HENSON, GATES & Co.

Sydney, Australia