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## Issuance of Securities in New York

New York Public Securities Commission

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[The following excerpts from the 1914 report of the division of capitalization of the New York public service commission (second district) are of considerable interest to those accountants who are brought into touch with the preparation of accounts and reports of corporations seeking authority for the issuance of securities. The report as a whole reflects great credit upon H. C. Hopson, chief of the division, and his staff.—*Editor, THE JOURNAL OF ACCOUNTANCY.*]

### PHASES OF CAPITALIZATION

The revised rules of the commission, particularly rules Nos. 19 and 24, are sufficiently explicit so that applications filed in compliance with their requirements contain practically all the data which the petitioners are required to submit for the consideration of the commission. Heretofore considerable correspondence has been necessary in order to obtain information and evidence now required by the rules. It is believed that the progress of such applications on account of the completeness of the information furnished will be subject to less delay than has heretofore been experienced.

Several applications for authority to issue securities with which to acquire the plant and property, or securities, of other corporations engaged in the same business in adjoining localities have been passed upon by the commission. In many such cases it is found that the purchasing corporations are obliged to pay a price somewhat in excess of the original cost of the physical property. The difference in price involves the strategic advantage of the vendor, the possibility of competition, and in most cases the business which has been developed. The commission has found it to be for the best interests of all concerned to permit corporations with generating stations of large capacity which operate at a low cost to acquire small plants in their territory, especially when approved by local authorities. This results in some cases in the immediate retirement and abandonment of a considerable portion of the physical property acquired. To limit the purchasing corporation to paying for such plants only the inventory cost of the actual physical property which will remain after the changes have been made might occasionally prevent such transactions, many of which have shown large benefits to all concerned. In cases where there has properly appeared any difference between the inventory cost of the physical property to be taken over and the price authorized to be paid therefor, such difference shall be amortized or charged off from earnings during a reasonable period of years. This practice is working out satisfactorily because it eventually results in a conservative statement of the property accounts of the acquiring company and at the same time makes possible an immediate putting into effect of the savings resulting from the progress of the art, large scale production, and reduced administrative expense.

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The commission is required to pass on the forms of mortgages and other trust indentures given by public service corporations. The current financial depression illustrates that a strong agency for the encouragement of conservative management and the protection of the credit of supervised corporations is that the mortgage debt of the companies shall be secured by an agreement which, so far as may be, insures that the earnings of the corporation shall in the first instance be applied toward the full maintenance of the mortgaged property, including a proper allowance for wear and tear, obsolescence and inadequacy. In requiring the indentures before approval to contain suitable clauses covering these and allied matters, the commission has had the uniform co-operation of corporations, bankers and trust companies. The Investment Bankers' Association has recommended certain standard provisions to go into equipment trust indentures which will result in a closer supervision of the pledged equipment by the trustees under the agreements.

In last year's report attention was called to the lack of care in the preservation of important vouchers, contracts, and other records by many corporations. This condition has not improved. While the better managed corporations are alive to the value of preserving their early records, many documents which are of vital importance in establishing the integrity of capital accounts are mislaid and eventually lost, largely on account of carelessness and unsystematic filing systems. Unless the matter receives better attention, the requirements of the uniform systems of accounts should be amplified by making the preservation of such records mandatory.

The methods of filing vouchers of many public service corporations are very unsatisfactory. Some file alphabetically by names of payees: this is objectionable from the standpoint of review or audit, for the reference may not be sufficiently definite to enable the prompt finding of the voucher in question. Others file in numerical order by months, beginning with a new number each month: this results in confusion. Others re-number vouchers each year: this is better, but confuses vouchers of different years. A very satisfactory method, and one which is followed by a majority of the corporations, is to number the vouchers consecutively until the numbers run to five figures and then begin over again. Corporations whose vouchers are kept in this manner can be examined with less irritation to their accounting departments and at a much less expense to the state.

Many corporations separate the evidence of payment from the original invoice, the treasurer retaining the former and the accounting department the latter. Frequently, even in one office, the invoices and cheques are filed separately. This is not good practice, as it is desirable that the invoice and the evidence of its payment should be together. Receipts for the canceled cheques can be furnished the treasurer by the accounting officer if desired.

Many corporations have their own form of invoice which the supply house is required to use. This has been found to be unsatisfactory,

as each manufacturer or supply company usually has the form of invoice best suited to its business. Furthermore, its employees are trained in preparing statements on such forms. When the form of some public service corporation is used, not infrequently the information furnished is insufficient. It is also wasteful. All the advantages of a uniform voucher are secured by using backers attached to the invoices received.

The uniform systems of accounts which have been adopted by this commission require that throughout all capital accounts the first entry in respect of any particular thing shall describe it with such particularity as to lead to its immediate identification. No serious attention is paid by many corporations to this fundamental requirement. For so-called "statistical" accounts such as meters, transformers, etc., or "inventory" accounts such as tools and implements, office furniture and fixtures, etc., the original invoices, duly receipted, usually contain sufficient information. In the case of expenditures for additions and betterments to buildings or to continuous structures, railroad track, electric line, pipe line and similar matters, it is essential that a record shall be kept by projects. Charges to a fixed capital account of a portion of a payroll, various quantities of materials, etc., do not enable an examiner to form an intelligent conception of the character of the expenditures, and yet many promiscuous charges of this sort are dumped into capital accounts which cannot be justified later.

Similarly, some steam railroad corporations make large expenditures for miscellaneous betterments to equipment without recording the particular cars on which such expenditures were made. While the commission was very liberal in imputing good faith to charges of this character for the first few years after its classifications of accounts had been promulgated, it should be clearly understood that this leniency cannot be expected to continue, and also that the intent of the capitalization provisions of the statute is that the applicant shall prove that the expenditures were for a proper capital purpose.

In making examinations of corporations the most important source of information, other than the accounts of the corporations themselves, is the inventory of the physical property in service at the conclusion of the examination. This statement of so-called physical data is taken from the sworn annual reports filed by the corporations with the commission. When the examiner has concluded his work the report of the examination, together with the annual report of the corporation to the commission, is referred to the commission's engineer to ascertain what, if any, property charged on the corporation's books is no longer in service. Conclusions drawn from the data as reported by the corporation are frequently found to be erroneous by reason of an utter lack of accuracy in the compilation of the data of physical property which is required by the report. When this fact is called to the attention of a corporation it usually states with absolute ingenuousness that the annual report is wrong. The fact that this is

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the sworn annual report required to be filed by the public service commissions law should be more impressive.

While some corporations complain against the alleged elaboration required by the annual report, from the experience of the division of capitalization were it not for the requirements of the reports to the commission and to the state tax commission little or no physical data whatever would be kept, though such a statement is almost unbelievable to the officials of the better managed corporations. In fact, it is in many cases literally impossible to secure any information whatever from the records of the corporation as to the amount of existing physical property prior to the time the filing of these reports was required.