Journal of Accountancy

Volume 17 | Issue 3 | Article 9

3-1914

# Correspondence

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# Correspondence

## Department Store Accounting

*Editor, The Journal of Accountancy:*

Sir: In reading the article entitled *The Accountant's relation to Inventory*—an extract from HENRY C. MAGEE'S *Department Store Accounting*—I was surprised to notice therein two glaring errors of accounting principle.

On page 444 of THE JOURNAL for December the following extract appears in connection with the author's treatment of goods received into stock in the latter part of a fiscal period, such goods being required for a future season's trade:

> Neither are the invoices charged to purchases—thus neither goods nor invoices are considered among the assets and liabilities of the business. This is proper if the goods are for the succeeding season.

It is a well-established principle of accountancy, in Canada at least, that all goods in stock or in storage, delivery of which has been accepted, must be included in assets and liabilities, for the reason that the acceptor is liable to the shipper even though the goods be destroyed by fire. The liabilities to creditors are increased by the invoice amount of such goods; consequently, a corresponding amount must be added to inventory. On page 449 of THE JOURNAL Mr. MAGEE says:

> The turnover is generally reckoned by dividing the average stock at cost into the total sale instead of purchases. As comparative profits and expenses are figured for reasons of convenience on the basis of sales, the turnover is also taken on that basis and the result is the same in either case, when brought down to gross profit.

Turnover of stock based on purchases or sales, divided by average inventory, is fundamentally wrong as a mathematical proposition, and no reason of convenience should excuse comparisons made on such bases.

Turnover of stock is ascertained by dividing the cost of goods sold by average inventory—that is to say: add together the inventory at the beginning and the purchases for the period. From this total subtract the inventory at the end of the period, and the result is cost of goods sold. Divide this by the average of the two inventories at the beginning and end of the period respectively.

We professional accountants cannot be too careful in making sure that any statements made or published by us are sound in principle.

It is with this fact in mind that I beg to draw Mr. MAGEE'S attention to these points.

Yours truly,

A. E. MIDDLETON HOPE, C.A.

Montreal, Dec. 29, 1913.

## *Correspondence*

*Editor, The Journal of Accountancy:*

Sir: Answering Mr. HOPE's criticism on the subject of goods received during the last part of the fiscal period I do not think Mr. HOPE expresses exactly what he means; but in my opinion there would be no violation of accounting principles whatever for the following reasons:

1. If the invoices are not shown amongst the liabilities nor the goods amongst the assets the effect on the profits would be the same as if both were included at face value—it will be recalled that the article provided that the goods would not be distributed (but held in the custody of the receiving room).

2. No accounting principle is violated, but rather, is conserved if the goods are worth the invoice cost, and as a rule they are worth more, being advance merchandise on which certain of the preliminary expenses have been paid, thus increasing the asset value without increasing the liability. We specially stated that the principle would not apply to past seasonable goods—furthermore each season should as far as practicable stand on its own basis to obtain the benefits of comparison of turn-overs, etc.

3. Insurance is usually figured on the average amount of stock carried—not only in inventory, *et seq.*, but goods invoiced on consignment, goods held in trust, goods sold but not delivered, etc., and for which the insured may be liable in case of loss; therefore inventory, as commonly understood, is not the only basis for merchandise insurance.

4. An auxiliary record of these goods and invoices is kept for application to the new period so that the items must balance out in order to clear the record. Special attention was called to "last minute items."

Turnovers, like expenses, are often figured on the basis of sales for the purpose of convenience, but that does not necessarily argue against correctness. Profit is always finally figured on the investment, although comparatively figured on the basis of sales. The selling price can be much better ascertained than the cost, and cost is never absolutely known until the business is settled up and cashed. We stated: "The result is the same in either case when brought down to gross profit on merchandise investment." Let us take an example:

Assuming an investment in merchandise,—that is an average stock for a fiscal period,—of $25,000, with a total turnover (sales) of $100,000, the times turned would be four, as figured average stock into sales. Say that the cost of the goods sold is $75,000, the *actual* times turned would be three. However, taking the four times at 25% profit, the result is 100% gross profit on amount turned, (which is the investment) namely, $25,000, or $25,000 profit. Then taking the three times turned at a profit of 33 1/3% on the cost—(as goods costing $75,000, sold for $100,000, would be sold at the rate of 33 1/3% profit on the cost), the result is 100% gross profit on the amount turned; also, $25,000, making the profit likewise $25,000, or reaching the same result by both methods.

It is not proper to figure turnover by taking "the average of the two inventories at the beginning and end of the period respectively," as stated by Mr. HOPE, because the inventory is frequently taken in the dull times when stocks are low, often much lower than the average, and it is the average stock which requires the financing and which costs the interest. Therefore in all up-to-date retail establishments the stock is estimated at frequent periods of the year, (sometimes as many as forty-eight times), and the average of all these stock estimates is taken as the average amount of money invested in merchandise—the inventory represents the investment in merchandise at inventory time only. While this might by a co-incidence be the same as the average for the entire period, it is most unlikely that it would be so.

Very truly yours,

HENRY C. MAGEE.

Philadelphia, Jan. 20, 1914.

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## Business Standing and Doings

*Editor, The Journal of Accountancy:*

Sir: I am enclosing a statement which from an accounting standpoint is unique to say the least. This is an actual copy of a statement submitted to us showing the activities of business which we examined about two years ago. In this connection a few words of explanation are in order:

Statement of business standing: By bills receivable in the statement is meant "open accounts receivable." "Checks not cashed" were post-dated checks; "inventory estimated" is an estimate of the equipment.

Statement of business doings: By the inventory of March 17, 1908, $3,438.97, is meant the value of the equipment of the concern at said date:

These statements were prepared by a bookkeeper of this concern who had not had any instruction in accountancy, as I am informed, but who had studied out this method for himself. At the time we made the examination he was over 62 years. Our examination confirmed the fact that the result as shown by these statements was correct.

I thought this might possibly be of interest.

Yours very truly,

RALPH D. WEBB.

Minneapolis, Minn.

### SCRAP IRON COMPANY

STATEMENT OF BUSINESS STANDING

| | | |
|---|---|---|
| Feb. 15, 1910 | Mdse. on hand .............$ | 891.14 |
| " " " | Bills receivable ........... | 1,832.20 |
| " " " | Cash in bank .............. | 25,221.73 |
| " " " | Cks from A.G., not cashed | 2,168.03 |
| " " " | Notes on hand, not due ... | 5,886.71 |

| | | | | |
|---|---|---|---|---|
| " " " Inventory estimated ....... | | 2,500.00 | | |
| Total .................. | | $38,499.81 | | |
| Less Bills payable ............... | | 145.97 | | $38,353.84 |
| | | $38,353.84 | | |

Overdrafts by individual members:

| | | | | |
|---|---|---|---|---|
| M. R. | $ 2,558.37 ............... | | | |
| D. L. | 3,041.41 ............... | | | |
| M. L. | 3,506.43 ............... | | | |
| L. K. | 7,532.85 ............... | $16,639.06 | $54,992.90 | |

Capital March 17, 1908:

| | | | | |
|---|---|---|---|---|
| M. R. | $ 7,061.84 .............. | | | |
| D. L. | 10,506.00 .............. | | | |
| M. L. | 4,583.25 .............. | | | |
| L. K. | 12,442.25 .............. | | | 34,593.34 |
| Net Profit ...................... | | | $20,399.56 | |

Total Assets per share:

| | | | | |
|---|---|---|---|---|
| M. R. | Balance ..........................$ 4,503.47 | | | |
| | Profit ........................... 5,099.89 | $ 9,603.36 | | |
| D. L. | Balance ..........................$ 7,464.59 | | | |
| | Profit ........................... 5,099.89 | 12,564.43 | | |
| M. L. | Balance ..........................$ 1,076.82 | | | |
| | Profit ........................... 5,099.89 | 6,176.71 | | |
| L. K. | Balance ..........................$ 4,909.40 | | | |
| | Profit ........................... 5,099.89 | 10,009.29 | $38,353.84 | |

STATEMENT OF BUSINESS DOINGS

*February 15, 1910*

| | | |
|---|---|---|
| From March 17, 1908 to Feb. 15, 1910. | | Total Mdse. |
| By " " " on hand .....................$ | 23,141.33 | |
| Mdse. bought during the period .................. | 99,212.01 | $122.353.34 |
| Mdse. sold during period, by ledger .............$ | 168,928.66 | |
| Mdse. sold during period by cash ................. | 1,204.55 | |
| Mdse. sold during period on hand Feb. 15, 1910 ... | 891.14 | |
| Inventory on March 17, 1908 ..................... | 3,438.97 | 174,463.32 |
| Gross Profit ..........................................$ | | 52,109.98 |

From which deduct:

Individual weekly drawings ....................$ 13,860.00

| | | |
|---|---|---|
| Salary | 2,475.00 | |
| Feed | 918.69 | |
| Repairs | 646.47 | |
| Rent | 886.20 | |
| Telephones | 518.20 | |
| Light & Power | 517.54 | |
| Medical treatment (injured employees) | 418.80 | |
| Stationery | 127.35 | |
| Interest | 289.45 | |
| Miscellaneous expense | 2,247.62 | |
| Labor | 8,805.10 | 31,710.42 |
| Net Profit | | $ 20,399.56 |

Profit per share: M. R. $5,099.89; D. L. $5,099.89; M. L. $5,099.89; L. K. $5,099.89.

## As to Professionals

*The Editor, The Journal of Accountancy:*

Will some one please rise and explain some of the difficulties created for the would-be independent practitioner by the standards of professional ethics proposed by ultra-professional professionals?

In the first place what is a profession? It cannot embrace all occupations characterized by brain work and the absence of manual labor, else executives in merchandising and manufacturing would be regarded as professional men, to say nothing of the gentry who live by their nimble wits.

Is a profession a calling which in the evolution of social custom has come to be practiced by educated men who have first pursued a course of study in that body of organized, systematized knowledge which pertains to the subject in which they profess to be skilled and constitutes its science? If so, the learned professions may no longer be three only—theology, law, medicine. How about engineering and accountancy?

But isn't the poor word "profession" overworked? Isn't a profession just a calling or vocation behaloed and sanctified in its primeval days by people who wished to constitute themselves an aristocracy thereby? Has a comprehensive, unvague definition of the word ever been formulated?

But a more practical question is, How is our would-be practitioner to get—no, not business—a clientage? The February JOURNAL is emphatic, editorially, in the statement that "solicitation of any kind should not be countenanced." But without solicitation how can a man acquire a practice?

To be sure he may solicit immodestly, but may he not also present modestly his preparation and qualifications for a needed business service? May he not even solicit in such manner that he will not lose or jeopardize one whit of the personal confidence that is spoken of as the basis of the professional relation? And if he may solicit in person with propriety, why not by means of letters or announcement cards sent through the mails?

What is the alternative? Shall he repress his spirit of enterprise, bank the precious fires of youth, and give over his conviction that it is his privilege to play a large and useful part in our world? Shall he stifle the spirit of adventure which lures him to the discovery of the need that his mind and soul can supply? Shall he violate the law of service by refusing to seek his opportunity for service? Shall he sit in his office twirling his thumbs, waiting, Micawber-like, for something to turn up? Does nature love an economic vacuum in the early years of a professional man's life?

Come, brethren, come out upon these white pages—behind the mask of a nom de plume if you must—and tell our imaginary entrant, who will no longer accept your salary because of the larger faith that is in him, how to remain dumb and yet acquire a practice! Like good sportsmen let us applaud his fine spirit, but let us also justify to him our creed that to rise to the high heights of professional ethics he must willingly suffer paralysis of enterprise, strangulation of initiative, and ultimate financial dissolution.

To this practical question our hypothetical candidate *solicits* a practical answer.

Yours very truly,

A. W. Weight.

New York, Feb. 27.